Supreme Court, U.S.
FILED
NOV 18 1992

No. #

IN THE SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1992

SANDERS CONFECTIONERY PRODUCTS INC., a Michigan Corporation; JOHN M. SANDERS; FILIPP KREISSL

Petitioners

SAM J. MERIGIAN, on behalf of himself and all persons who were shareholders of Sanders Confectionery Products Inc., as a class action under FRCP 23(a) and 32(b)

Petitioners

vs.

HELLER FINANCIAL, INC., a Delaware Corporation; BUTZEL, KEIDEN, SIMON, MYERS & GRAHAM, a partnership; JOHN WM. BUTLER JR., JAY ALIX

Respondents

PETITION FOR WRIT OF CERTIORARI
UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

Richard L. Roble JD, PC
Richard L. Roble
P.O. Box 10033
1719 Abercorn St.
Savannah, GA 31412
(912) 232-7722

QUESTIONS PRESENTED:

1. Whether the Court erred in holding the Petitioners' non-core issues that are related to the bankruptcy could be adjudicated by the Bankruptcy Court with a jury trial.

2. Whether a litigant is required to file in Bankruptcy Court and have the Bankruptcy Judge find that the claims are "non-core" and find no subject matter jurisdiction in the face of a jury demand or in the alternative may the litigant file the case directly in District Court,

3. Whether the Court erred in while holding that the Petitioner stockholders claims were not barred by res judicata or collateral estoppel and hence that the right to a jury trial is not an issue, that the stockholders failed to properly plead that the Respondent Heller was "control person" over the public stock offering thereby dismissing their case for failure to state a claim.

TABLE OF CONTENTS

Questions presented i,3

Citation of Authorities iii

Opinion below 2

Constitutional Provisions 3

Statement of the Case 4

Reasons for Granting the Writ 10

Argument. Question 1 13

Argument. Question II 17

Argument . Question III 21

Conclusion

Appendix - 1 - Opinion of the Court of Appeals for the Sixth Circuit

Appendix -2 - Opinion of the District Court for the Eastern District of Michigan

Appendix-3 - Excepts from the Petitioner's complaint pleading "control person"

CITATION OF AUTHORITIES

Name	page
CONSTITUTIONAL PROVISIONS	
Fifth Amendment	15
Seventh Amendment	(no specific page)
CASES	
Ben Cooper, Inc. v Insurance Company of the State of Pennsylvania et al, 924 F2d 36, 1991 US App LEXIS 994, 24 Collier Bankr. Cas 2d (MB) 861,	10,11
Connecticut National Bank v Germain 112 S. Ct. 1146; 1992 U.S. LEXIS 1531; 117 L. Ed. 2d 391, 1992	11
Granfinanciera, SA vs Norberg, 492 US 22, 109 S. Ct. 2782, 106 L. Ed 2d 26 (1989)	10,11,13,19
In Re Diasonics SEC Litigation, 599 F. Supp 447 (ND Cal 1984).	24
In Re Maislin Industries vs. Certified Brokerage System, et al., 75 Bankr. 170 (E.D. Mich. 1987)	18
In Re Kaiser Steel Corp , 911 F2d 380, (10th/ Cir. 1990)	20

Jett v Sunderman, et al, 840 F2d 1487 (9th/ Cir. 1988) 24

Lagenkamp v C. A. Culp, 498 U.S. 42; 111 S. Ct. 330; 1990 U.S. LEXIS 5745; 112 L. Ed. 2d 343; 11

Metge v Baehler, 762 F2d 621 (1985) 21,22,23,24

Moore v Fenex, Inc., 809 F2d 297 (6th/ Cir. 1986) 25

Northern Pipeline Constr. Co. vs Marathon Pipe Line Co., 458 US 50, 73 LEd2d 598, 102 S. Ct. 2858 (1982), 11,15

Securities and Exchange Commission v Coffey, 493 F 2d 1304 (6th. Cir. 1974) 24

STATUTES AND RULES

15 USC 77o 22

28 USC 151 (1988) 13

28 USC 157 20

28 USC 157 (b), 13,16,18

28 USC 158(a). 16

28 USC 157 (C), 13,14,16

28 USC 1334 (Supp. II 1984). 20

FRCP 8 22

FRCP 12(b)6 21,24

OTHER

"Federal Constitutional Right to Jury Trial in Proceedings Involving Bankruptcy or Receivership - Supreme Court Cases", 106 L. Ed2d 652 11,12

H.R. Rep. No. 1383, 73rd Cong., 2d sess. 26 (1934). 22

Federal Judgeship Act of 1984 , 15

INTRODUCTION: The Petitioners, Sanders Confectionery Products Inc. and Sam Merigian, et al., respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Sixth Circuit, entered in the above styled proceeding on August 17, 1992. [1]

OPINIONS BELOW: The opinion of the Court of Appeals for the Sixth Circuit reported at 973 F2d 474, 1992 US App LEXIS 18758, is reprinted in the Appendix at App. 1.

The opinion of the United States District Court for the Southern District of Michigan, Ann Arbor, has not been reported. It is reprinted in the Appendix at App. 2.

JURISDICTION: Invoking jurisdiction under 28 USC 1331 and federal questions, the Petitioners bought suit in the United States District Court for the Southern District of Michigan requesting a jury trial.

---

[1] The Sixth Circuit treated the filings case of SCPI et al under file 90-2039 and the case of Merigian under 90-2040. The Sixth Circuit consolidated the two cases for appellate purposes and issued one decision. For the purpose of this Petition for Cert. the cases are still consolidated.

CONSTITUTIONAL PROVISIONS INVOLVED:

Seventh Amendment, United States Constitution

In Suits at common law where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved . . .

Fifth Amendment, United States Constitution

. . . . Due process . . .

QUESTIONS PRESENTED:

1. Whether the Court erred in holding the Petitioners' non-core issues that are related to the bankruptcy could be adjudicated by the Bankruptcy Court with a jury trial.

2. Whether a litigant is required to file in Bankruptcy Court and have the Bankruptcy Judge find that the claims are "non-core" and find no subject matter jurisdiction in the face of a jury demand or in the alternative may the litigant file the case directly in District Court,

3. Whether the Court erred in while holding that the Petitioner stockholders claims were not barred by res judicata or collateral estoppel and hence that the right to a jury trial is not an issue, that the stockholders properly failed to plead that the Appellee Heller was "control person" over the public stock offering thereby dismissing their case for failure to state a claim.

RULE 28.1 LIST: Sanders Confectionery Products Inc. is a publicly held corporation with its principal offices in Detroit, Michigan. with some 3,000 stockholders sought to be represented by Sam Merigian as a class.

Heller Financial, Inc. is a privately held corporation incorporated in Delaware with its principal offices in Chicago. It is believed to be owned by Fuji Bank of Japan.

STATEMENT OF THE CASE: Petitioners Sanders Confectionery Products, Inc., et al ("SCPI") and their stockholders, sought to be represented by Sam Merigian's, appeal from the district court's dismissal of their lender

liability claims and security claims against Heller Financial, Inc.,et al.

All of the Petitioners assert the District Court erred in holding that the earlier bankruptcy proceedings of Fred Sanders, Inc. barred these actions under the doctrine of res judicata. Fred Sanders Inc., the debtor is the wholly owned subsidiary of the publicly held corporation, Sanders Confectionery Products Inc. (SCPI), but SCPI did not file a claim in the Bankruptcy Court. Merigian, on behalf of the stockholders [2] claims the district court erred in failing to recognize Heller's liability as a control person under section 12(2) of the 1933 Securities Act.

In late 1985, Filipp J. Kreissl, president of Sanders Confectionery Products, Inc. (SCP!), approached Heller Financial, Inc. (Heller), a commercial funder, to seek financing for Fred Sanders, Inc. (FSI). SCPI was the parent company of FSI, a 117 year old company famous in southeastern Michigan for its hot fudge and chocolate candies. FSI had recently emerged from bankruptcy

[2] Sam Merigian sought certification of the 3,000 stockholders and if remanded, will continue to seek certification of the class,

protection and sought to expand its operations. In a February 15, 1986 loan agreement, Heller agreed to provide up to $2.45 million to the candy manufacturer, but due to manipulation of the lending formulas, Heller never lent the full amount of the money.

Therefore, in need of further financing , SCPI began preparing a stock offering in December 1986. On December 9, 1986, Heller certified in the offering circular that SCPI - FSI was a borrower in good standing. However, after SCPI issued the prospectus, Heller found defaults in the payment of state and federal taxes. To avoid changing the prospectus, SCPI requested a waiver of these defaults by Heller. Heller conditionally agreed, upon a grant of further concessions by FSI and SCPI. The terms of the new agreement made Heller a "control person" under SEC code which becomes significant in the Merigian claims.

Heller agreed to loan additional funds especially if the public offering was successful. The offering was successful raising some $5,000,000 and acquiring the 3,000 Appellant shareholders who are seeking certification as a class in this law suit. Despite the success of the offering, Heller defaulted

on their promise to loan additional funds and instead, found from time to time, purported "defaults" in the loan agreements which they cured or waived with more and more control being exercised over FSI and SCPI.

Heller closed its Michigan office commensurate with being acquired by Fuji Bank of Japan and informed SCPI and FSI that they no longer fitted its loan profile. The intentions of Heller to abandon SCPI were formed in early in 1987, but not disclosed to SCPI in time to allow them to secure another commercial funder for the Christmas season. [3]

Under promises of discretionary additional funding, Heller forced FSI file for Chapter 11 Bankruptcy and then secured control of the Bankruptcy with a post petition loan agreement. The post petition loan agreement made Heller a priority secured lender over all other creditors, but Heller never furnished the additional funding and instead forced the liquidation sale of FSI. Heller was the only creditor fully paid in the bankruptcy. With the exception of First Independence

---

[3] For the candy business, Christmas is the crucial season of the year directly effecting the success of the business. If there is no funding to acquire inventory to manufacture candy and confectionery products, it could mean the demise of SCPI and FSI.

National Bank, none of the other creditors received any payments.

In 1989 SCPI, Sanders, Kreissl and Sam J. Merigian, a shareholder of SCPI, sued Heller, Butzel, Keidan, Simon, Myers & Graham, Heller's attorneys, John W. Butler, a partner in the Butzel firm, and Alix, the bankruptcy trustee. The complaint contained thirteen counts alleging, among other things, common law fraud, RICO violations, and securities law claims. The district court dismissed all of the claims as barred on res judicata grounds, based on the bankruptcy case of Fred Sanders, Inc. The court also held that Merigian failed to state a claim upon which relief may be granted.

All discovery was denied during the pendancy of the summary motion to dismiss even though the Petitioners' filed numerous requests for discovery and for relief from an ill advised stay of discovery stipulation entered into by prior counsel. It was contended by the Petitioners' that discovery would have shown that Merigian properly plead a "control person" case and discovery would have revealed there was

no relationship with the FSI bankruptcy case. This showing would have defeated the Appellees defense of res judicata.

SCPI and Merigian contend that none of the other elements of res judicata have been met as to their claims. They argue that they were not a party, or in privity with a party in the bankruptcy for res judicata purposes. They assert that the only party to the FSI bankruptcy for res judicata purposes was the debtor FSI and that, while SCPI owned FSI, the two retained separate corporate identities. For these reasons SCPI could not be considered a party to the bankruptcy.

The Court of Appeals reversed the District Court and held that Merigian and his stockholders were not represented by SCPI and not in privity with any party in the bankruptcy. The Court of Appeals found that SCPI was an extended party to the Bankruptcy action , but reversed the District Court and held that the action was a non-core proceeding. The classification of non-core" significantly effects the jurisdiction of the bankruptcy court to adjudicate the claims of the Petitioners'.

REASONS FOR GRANTING THE WRIT

Importance to the National Jurisprudence

This petition for certiorari concerns the issue of jury trials in non-core cases "related to" bankruptcy actions. This Court affirmatively addressed the right to jury trials in certain claims in Granfinanciera, SA vs Norberg, 492 US 22, 109 S. Ct. 2782, 106 L. Ed 2d 26 (1989) without addressing whether the bankruptcy court had the authority to conduct jury trials in all cases.

Ben Cooper, Inc. v Insurance Company of the State of Pennsylvania et al, 924 F2d 36, 1991 US App LEXIS 994, 24 Collier Bankr. Cas 2d (MB) 861, vacated by the Supreme Court in 111 S. Ct 425 (1990) and remanded to address the issue of Appellate jurisdiction. The legal community was hopeful that Ben Cooper might resolve the question of whether the Bankruptcy Court had the Constitutional Authority as a Non-Article III Court to conduct jury trials. Instead the decisions focused on the appellate channels of interlocutory bankruptcy orders and ceased to focus on jury trial issues.

Presumably the procedural issue of appealing interlocutory bankruptcy orders was resolved by Connecticut National Bank v Germain 112 S. Ct. 1146; 1992 U.S. LEXIS 1531; 117 L. Ed. 2d 391, 1992 disposing of the narrow issue of appealability left open by Ben Cooper , but not addressing the issue of jury trials.

Granfinanciera opened the door to jury trials for adversary proceedings holding that the distinguishing enabling factor was whether the adversarial defendant filed a claim in the bankruptcy court thereby exposing himself to its exclusive equity jurisdiction and presumably waving the usual Article III court rights. Presumably, Lagenkamp v C. A. Culp, 498 U.S. 42; 111 S. Ct. 330; 1990 U.S. LEXIS 5745; 112 L. Ed. 2d 343; was granted Certiorari to explore the distinctions created in Granfinanciera entitling one to a jury trial in a core proceeding if a claim has been filed.

The controversy started with Northern Pipeline Constr. Co. vs Marathon Pipe Line Co., 458 US 50, 73 LEd2d 598, 102 S. Ct. 2858 (1982), which left the legal community in doubt; the issue remains unresolved. See "Federal Constitutional Right to Jury Trial in Proceedings Involving

Bankruptcy or Receivership - Supreme Court Cases", 106 L. Ed2d 652

There is a division among the Circuits regarding these questions. There is confusion in the legal community regarding the entire issue where to file a "non-core" proceeding which may have a relationship to bankruptcy matters while preserving the right to a jury trial afforded to actions at law. There is no definitive ruling on what court has the authority to classify the proceedings as "core" or "non-core" and at what stage of the proceedings does this classification take place. This is all compounded by the seeming reluctance of the Congress to legislatively address these issues. Therefore, the Petitioners respectfully submit that it is in the national interests of jurisprudence that this Court grant Certiorari.

Argument

I.

WHETHER THE COURT ERRED IN HOLDING THE PETITIONERS' NON-CORE ISSUES THAT ARE RELATED TO THE DEBTORS BANKRUPTCY COULD BE ADJUDICATED BY THE BANKRUPTCY COURT WITH A JURY TRIAL.

At the present, there are no specific procedures in the Bankruptcy Rules providing for a jury trial. Since Granfinanciera suggests, without clearly holding, that the adjudication of core proceedings under 28 USC 157(b) grants the authority to grant final judgments and under the doctrine of necessity suggested by 28 USC 151 (1988), a bankruptcy court may be authorized to conduct jury trials in some instances. This line of reason confronts 28 USC 157 (C), which states that in cases of non-core issues that are related to a bankruptcy, the bankruptcy court may hear [4] the matter and submit proposed findings of fact and conclusions of law to the district court, but may not make final decision on the matter without the consent of the parties,

[4] (Emphasis added) The use of the term "may" is permissive and suggests that the District Court has primary jurisdiction.

suggesting that the Bankruptcy Court would not have the authority to conduct jury trials. The effect of the conduct of the Petitioners' in filing their action in the District Court was that they did not wish to effect a waiver under 28 USC 157(C) to an Article III forum and that they specifically wished to exercise their right to a jury trial. In an ordinary tort action, the fact that the right of a trial by jury is guaranteed by the Constitution is so obvious that it hardly needs belaboring.

The effect of this in the case sub judice is that the District Court and the Court of Appeals based the granting of the Appellees motion for summary disposition upon the theory that the matters were either res judicata or collaterally estopped and that the action should have been filed in the bankruptcy court. If this Court holds that the bankruptcy court had no authority to conduct jury trials in non-core matters, then the entire premise upon which the granting of the motion to dismiss is based is in error and the case must be reversed. [5]

---

[5] The four elements of res judicata or collateral estoppel would not be met if the FSI bankruptcy court did not have jurisdiction to hear any of the Appellants' claims.

The four elements are; (1)the precise issue raised in the present case must have been raised and actually litigated in the prior proceedings; (2) determination of the issues must have been necessary to

Due Process is afforded a party under the Fifth Amendment to the Constitution and is applicable to both civil and criminal proceedings. In 1989, when this law suit was originally filed in the District Court, there was no practice of jury trials in Bankruptcy Court. For guidance the legal community had Northern Pipeline Constr. Co. vs Marathon Pipe Line Co., 458 US 50, 73 LEd2d 598, 102 S. Ct. 2858 (1982), which gave the bankruptcy court jurisdiction over all civil proceedings arising under, arising in or related to cases under title 11. The Bankruptcy Courts were not afforded Article III status. The Supreme Court held that Congress could grant the authority to the Bankruptcy Court to issue final orders in "core" matters, it could not issue final orders in traditional law claims. Those were reserved for Article III courts.

Pursuant to Congress' Bankruptcy Amendments and the Federal Judgeship Act of 1984 , the statutory scheme attempted to delineate the scope of the bankruptcy court's

---

the outcome of the prior proceedings ; (3) the prior proceedings must have resulted in a final judgment on the merits; and (4) the party against whom estoppel is sought must have had a full and fair opportunity to litigate the issue in the prior proceeding. [Citations omitted]

power to hear and resolve disputes, the bankruptcy judges have plenary powers of adjudication over core proceedings. See 28 USC 157 (b), 158(a). With respect to non-core matters, however, a bankruptcy judge's findings of fact and conclusions of law are subject to de novo review by the district court. See 28 USC 157(c). Consequently, the determination of whether a matter is core or non-core may dictate in what forum, an Article III or and Article I Court, a particular dispute will be heard and resolved.

While the Court of Appeals correctly characterized the Petitioners' claims as non-core they erroneously implied that Petitioners' claims should have been adjudicated by the FSI Bankruptcy Court.

The law is replete with authority that the Bankruptcy Court can not conduct jury trials in "non-core but related cases". The secondary issue then becomes is a litigant required to file in Bankruptcy Court and have the Bankruptcy Judge find that the issue is non-core and find no subject matter jurisdiction in the face of a jury demand or may the litigant file the case in District Court,

II.

WHETHER A LITIGANT IS REQUIRED TO FILE IN BANKRUPTCY COURT AND HAVE THE BANKRUPTCY JUDGE FIND THAT THE CLAIM IS "NON-CORE" IN THE FACE OF A JURY DEMAND OR IN THE ALTERNATIVE MAY THE LITIGANT FILE THE CASE DIRECTLY IN THE DISTRICT COURT.

While the Petitioners' were not required to plead that their action was non-core, they filed it in the District Court with a jury demand under the premise that the Bankruptcy Court lacked subject matter jurisdiction. The District Court found the claims to be "core", but the Court of Appeals reversed that finding and held the claim, while "non-core", was related to the FSI bankruptcy.

The Court of Appeals erroneously held that since the matter was related to the debtor's bankruptcy, it should have been filed in bankruptcy court regardless of the effect of "core" - "non-core" classification and consequently found the Petitioners' claims barred by the doctrine of res judicata.

While due process is often contemplated in the context of criminal proceedings, it also applies as well in the civil context. In 1987, just before the Debtor filed bankruptcy, Judge Steven W. Rhodes, United States Bankruptcy Judge for the Eastern District of Michigan [the chief Bankruptcy Judge in Detroit where FSI subsequently filed bankruptcy] issued an opinion on subject matter jurisdiction which Michigan practitioners relied on for guidance. In Re Maislin Industries vs. Certified Brokerage System, et al., 75 Bankr. 170 (E.D. Mich. 1987) held that a third party did not have subject matter jurisdiction to maintain its claim in the bankruptcy court where the proceeds from the intended litigation would not benefit the debtor or the debtor's estate.

The Petitioners' did not appear in the FSI bankruptcy action, were not a creditor of the debtor, did not file any claim in the bankruptcy action [6] and their claims were not enumerated in the listing of "core" actions under 28 USC

---

[6] Jack Sanders, one of the Appellants did file a claim in the bankruptcy but SCPI and the stockholders did not. SCPI did submit a plan of reorganization as did other enterprises but that did not make them a "party" in the bankruptcy in the strictest sense. Since the Appellants claim would effect the integrity of the relationship between the Debtor, FSI and its creditor, Heller, the Court of Appeals/ Circuit found that while not a core proceeding, there was relationship.

157(b)(2). Since the Petitioners' maintained they were not a strict party and the proceeds of successful litigation would not benefit the administration of the estate of FSI, the Bankruptcy Court lacked subject matter jurisdiction, they filed their action in the District Court.

Furthermore, the Petitioners' were not collaterally attacking any of the orders of bankruptcy, but rather arguing that these orders established their "injury" or "damages" in the District Court common law action.

The Petitioners' did not subject themselves to the jurisdiction of the Bankruptcy Court even prior to Granfinanceria.

Coincidentally, SCPI did file a motion in the Bankruptcy Court at the same time it filed its law suit in the District Court to remove the Trustee, Jay Alix for a previously undisclosed conflict of interest. The Bankruptcy Court sua sponte withdrew reference on that replacement motion and remanded it to the District Court. [7]

---

[7] The District Court after dismissing the main law suit, sent the replacement motion back to the bankruptcy court for adjudication holding that it was not barred by the principles of res judicata.

The District Court sits as the original jurisdiction in bankruptcy. and would be empowered to make the determination whether proceeding is core or non-core under 28 USC 157. In Re Kaiser Steel Corp , 911 F2d 380, (10th/ Cir. 1990) While the Bankruptcy Court may classify an action as core or non-core , there is nothing precluding the District Court's ability to classify a proceeding where the bankruptcy court has not already done so. After all, Congress vested jurisdiction of bankruptcy matters in the District Courts pursuant to 28 USC 1334 (Supp. II 1984).

It may be argued the most the District Judge sitting as the court of original jurisdiction could have made the determination that the Petitioners' claim was core and then remanded the case to the Bankruptcy Court for adjudication. The draconic action of dismissing the case given the circumstances was error. .[8]

---

[8] This argument is presented in the alternative. District Judge LaPlata did find the claim was "core" and could have remanded the case to the Bankruptcy Court for adjudication like he did the motion to replace the trustee. Parenthetically, the District Judge was reversed on his finding that the claim was "core".

Judicial economy demanded that the claim be filed in the District Court which has original jurisdiction.

III.

WHETHER THE COURT ERRED IN HOLDING THAT THE STOCKHOLDERS FAILED TO PROPERLY PLEAD "CONTROL PERSON" AND DISMISSED THE PETITIONERS' CASE FOR FAILURE TO STATE A CLAIM .

The Court of Appeals reversed the District Court and found that the stockholders who bought the SCPI public stock were not, as a matter of law, represented in the FSI bankruptcy and therefore the doctrine of res judicata would not bar their claim.

Instead the Court of Appeals decided under the standard of FRCP 12(b)6 that the Petitioners' failed to state a claim. upon which relief can be granted The Court held that under the guidelines of Metge v Baehler, 762 F2d 621 (1985) the Appellant stockholders complaint failed to properly allege "control person."

Since the issue was decided under FRCP 12(b)(6), the Petitioners' should have been given the opportunity to amend their complaint rather than face the harsh remedy of dismissal.

The test should have been notice pleading under FRCP 8 and since there was no discovery permitted during the motion practice of this case, the Petitioners' should have been given the benefit of the doubt.

The Court of Appeal's absolute reliance on Metge is not permissible. Examining Metge, the court held that the "control person" statute, 15 USC 77o is to be construed liberally and stated, " Congress has provided little guidance for the Courts in construing these sections, however, believing that strict definitions of control would be "undesirable" because it would be difficult if not impossible to enumerate or to anticipate the many ways in which control may be exerted." The authority for this remark came from the legislative intent. H.R. Rep. No. 1383, 73rd Cong., 2d sess. 26 (1934).

The case law on "control person" requires some actual participation in the corporation's operations to impose liability. The level of participation and its effect would presumably be on a case by case basis. Metge was decided on a motion for summary judgment, after discovery. In Metge it had been determined that there was no evidence produced which showed actual control. The standard of a motion for summary judgment under which Metge was decided distinguishes it from the case sub judice.

The Court of Appeals took the two prong test discussed in Metge as dogma, to wit; (1) that the defendant lender actually participated in (exercised control over) the operations of the corporation in general and (2) the defendant possessed the power to control the activity upon the which the primary violation is predicated.

This finding is error; the sections dealing with "control person", Portions of Counts III, IV , V and VI are attached here as "Appendix 3". and the complaint demonstrates beyond cavil that the Metge allegations were made.

There are numerous allegations made between paragraphs #235 and #319 that Heller (the control person) did control all the cash flow of SCPI and FSI. Heller received all the cash income from sales and controlled all the disbursements made by FSI and SCPI. In practice, SCPI and FSI could only pay the bills Heller approved. In addition, if the corporate operations were not in accordance with Heller's wishes, they would be funded. In effect, Heller controlled the day to day operation of SCPI and FSI.

The next aspect of the Metge test is whether the defendant possessed the power to control the activity upon the which the primary violation is predicated.

Heller is liable as a "control person" when it controls those who are primarily liable for securities law violation. Liability attaches only if Heller had actual power or influence over the allegedly controlled person and was a culpable participant in the alleged illegal activity. Jett v Sunderman, et al, 840 F2d 1487 (9th/ Cir. 1988)

The issue of a "controlling" person is a question of fact which is not capable of adjudication under FRCP 12(b)6. See Re Diasonics SEC Litigation, 599 F. Supp 447 (ND Cal 1984).

Heller, never disputed that it concealed material information from the purchasers of the stock, but argued they were under no duty to disclose it because of lack of privity with the purchasers. The common law refutes that argument. Heller knew that the purchasers would rely on their representations in making their stock purchases.

The Petitioners' maintain that Heller had a hidden agenda. The hidden agenda was to put a solid financial base under SCPI, have successful public offering and then terminate the funding by forcing FSI into a liquidation bankruptcy where they were assured of being fully paid because of their super priority position, all resulting in rendering the stockholders' investment as worthless

There is no dispute that Heller furnished information used in the preparation of the prospectus. A person undertaking to furnish information which is misleading

because of a failure to disclose a material fact or a subsequent material change of circumstances is a primary participant.

The decisions of Moore v Fenex, Inc., 809 F2d 297 (6th/ Cir. 1986) and Securities and Exchange Commission v Coffey, 493 F 2d 1304 (6th. Cir. 1974) removed any possible "privity" issue that Heller may maintain since they never had "direct" contact with any of the purchasers. Since Coffey had supplied some material information which was misleading because of omissions of fact, the Court held that he could be liable as a primary participant.

Since Heller made the initial disclosure in the preparation of the prospectus, it was obligated to inform the potential investors and the Securities and Exchange Commission of any material change in circumstances. Since there were material change in circumstances while the offering was "alive" which were not disclosed, there was a violation of Rule 10(b)5.

In addition to being a "Controlling party" under the Securities Act, Heller also "controlled" the information. The information sought for purposes of the prospectus was within

the exclusive province of Heller and it controlled what information was disseminated.

Therefore the action of the Court in dismissing the Appellant Stockholders' complaint for not properly pleading "control person" was clearly in error and should be reversed.

CONCLUSION: Because of the unique question presented relative to the issue of jury trials in bankruptcy courts and the selection of the proper forum, this case is does have an effect of the body of law effecting the national jurisprudence and this Petition for Certiorari should be granted.

Respectfully submitted,

Richard L. Roble JD, PC

BY _____
Richard L. Roble
Ga Bar #610900 - active
Mich. Bar # P19534 - active
Member U.S. Supreme Court Bar
P.O. Box 10033
1719 Abercorn St.
Savannah, Ga 31412
(912) 232-7722

APPENDIX - 1

Reproduced from LEXIS

SANDERS CONFECTIONERY PRODUCTS, INC., a Michigan corporation; JOHN M. SANDERS; FILIPP J. KREISSL, Plaintiffs-Appellants (90-2039), SAM J. MERIGIAN, on behalf of himself and all persons who were shareholders of Sanders Confectionery Products, Inc., as a Class Action Under FRCP 23(a) and 23(b), Plaintiff-Appellant (90-2040), v. HELLER FINANCIAL, INC., a Delaware corporation; BUTZEL, KEIDAN, SIMON, MYERS & GRAHAM, a partnership; JOHN W. BUTLER, JR.; JAY ALIX, Defendants-Appellees. Nos. 90-2039, 90-2040 UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT 973 F.2d 474; 1992 U.S. App. LEXIS 18758; Fed. Sec. L. Rep. (CCH) P96,966

November 19, 1991, Argued

August 17, 1992, Decided

August 17, 1992, Filed

PRIOR HISTORY: [*1] On Appeal from the United States District Court for the Eastern District of Michigan. District No. 89-60029. George LaPlata, District Judge.

DISPOSITION: AFFIRMED

COUNSEL: For SANDERS CONFECTIONERY PRODUCTS, INC., a Michigan corporation, JOHN M. SANDERS, FILIPP J. KREISSL, Plaintiffs - Appellants: Richard L. Roble ARGUED, BRIEFED, 912-232-2791, 301 W. York Street, P.O. Box 10033, Savanah, GA 31412.

For HELLER FINANCIAL, INC., a Delaware corporation, BUTZEL, KEIDAN, SIMON, MYERS & GRAHAM, a partnership, JOHN W. BUTLER, JR., Defendants - Appellees: Susan Artinian, 313-568-6585, Dykema & Gossett, 400 Renaissance Center, 35th Floor, Detroit, MI 48243-1595. Timothy J. Rivelli, 312-558-5600, Daniel K. Webb, ARGUED, BRIEFED, 312-558-5600, Winston & Strawn, 35 W. Wacker Drive, Suite 4200,Chicago, IL 60601.

For JAY ALIX, Defendant - Appellee: Sheldon S. Toll, 313-256-7800, Honigman, Miller, Schwartz & Cohn, 660 Woodward, Suite 2290 First National Building, Detroit, MI 48226. Robert J. Diehl, Jr., 313-259-7777, David G. Chardavoyne, 313-259-7777, Michael B. Lewiston, ARGUED, BRIEFED, 313-259-7777, Bodman, Long & Dahling, 100 Renaissance Center, 34th Floor, Detroit, MI 48243.

JUDGES: Before: NELSON and SUHRHEINRICH, Circuit [*2] Judges; and ENGEL Senior Circuit Judge.OPINION BY: ENGEL##

OPINION: ENGEL, Senior Circuit Judge. Plaintiffs Sanders Confectionery Products, Inc., John M. Sanders, and Filipp J. Kreissl appeal from the district court's dismissal of their lender liability claims against Heller Financial, Inc., Butzel, Keidan, Simon, Myers & Graham, John W. Butler Jr., and Jay Alix. Plaintiff Sam J. Merigian appeals from the dismissal of his RICO and securities fraud claims against Heller Financial, Inc. n1 All of the plaintiffs claim the district court erred in holding that the earlier bankruptcy proceedings of Fred Sanders, Inc. barred these actions under the doctrine of res judicata. Merigian claims the district court erred in failing to recognize Heller's liability as a control person under section 12(2) of the 1933 Securities Act and as an aider and abettor in violation of section 10(b) of the 1934 Securities Act. This case also presents questions concerning causation and standing to bring a RICO claim. We affirm the district court's dismissal of the actions by Sanders ConfectioneryProducts, Inc., Sanders, Kreissl, and Merigian.

- - - - - - -Footnotes- - - - - - - - - - - - - - - - - -

n1 Originally, Merigian joined in all of the actions against all of the defendants, but has since dropped the claims against all defendants except Heller Financial. The district court denied his motion to separate his claims from those of the other plaintiffs

----------End Footnotes----------

[*3]

I In late 1985, Filipp J. Kreissl, president of Sanders Confectionery Products, Inc. (SCPI), approached Heller Financial, Inc. (Heller) about obtaining financing for Fred Sanders, Inc. (FSI). SCPI was the parent company of FSI, a117 year old company famous in southeastern Michigan for its hot fudge and chocolate candies. FSI had recently emerged from bankruptcy protection and sought to expand its operations. In a February 15, 1986 loan agreement, Helle agreed to provide up to $ 2.45 million to the candy manufacturer. In July 1986 the relationship between Heller and FSI began to sour. Heller declared events of default, accelerated the loan and stopped funding. As a cure, Heller demanded loan guarantees from SCPI, Kreissl and SCPI's chairperson, John M. Sanders, a release of cure period rights, a "blocked account" for cash collections, and increased interest rates. The borrowing formula was to

remain unchanged. FSI acceded to these demands in order to obtain much needed funds to begin building an adequate Christmas inventory. Seeking more cash, and hoping to draw on its good reputation in Detroit, SCPI began preparing a stock offering in December 1986. On December 9, 1986, Heller[*4] certified that FSI was a borrower in good standing. However, after SCPI issued the prospectus, Heller found defaults in the payment of state and federal taxes. To avoid changing the prospectus, FSI requested a waiver of these defaults by Heller. Heller conditionally agreed, upon a grant of further concessions by FSI. Throughout this period, FSI sought changes in the lending formula as part of an effort to obtain additional funds. Finally, on or about February 17, 1987, Heller orally agreed to loan FSI an additional $ 750,000 if the public offering raised at least $ 1,000,000. The public offering, completed in May 1987, raised $ 5,000,000. Heller never made the additional funds available

On February 18, 1987, FSI received a letter from Heller declaring more events of default. FSI once again cured the default. FSI also obtained more funds through a $ 600,000 loan from First Independence Bank. Heller represented to First Independence that FSI was a borrower in good standing, but upon execution of the note Heller made

additional demands. It required payment of $ 120,000 from this loan, double its original demand, and accelerated the maturity date of its loan by eight months

In August [*5] 1987, the state of Michigan issued another tax lien, this time in error. First Independence and Heller declared and then rescinded events of defaults. Heller also closed its Michigan office, an event planned since at least May 1987. At this time Heller told FSI that small business loans no longer fit its plans, and informed FSI it should seek financing elsewhere.

Heller initially denied FSI a Christmas inventory loan, but in October offered one when FSI could not procure a loan from other sources. FSI prepared a debt offering for fall 1987, but the stock market crash delayed it. FSI remained cash hungry.

On November 5, 1987, Heller sent FSI another letter of default, and declared it would continue stop-gap financing on an absolutely discretionary basis. On November 9, FSI requested an additional $ 450,000 for Christmas needs. Heller promised to do everything it could, but then failed to attend a November 13 meeting on the topic. Instead, Heller foreclosed on its loans. The next day, Heller demanded FSI file for Chapter 11 protection and execute new loan agreements. FSI filed for bankruptcy on November 16, 1987

On November 18, 1987, FSI sought authorization to borrow more money from [*6] Heller. See 11 U.S.C. @ 364. The post-petition agreement gave discretionary financing to the Debtor (FSI) while waiving all claims, setoffs or defenses of FSI, SCPI, Sanders and Kreissl against Heller. The bankruptcy court entered a Consent Financing Order approving the post-petition agreement and ratifying the pre-petition agreements. Neither SCPI, Sanders nor Kreissl signed the Consent Order, but they were party to and guarantors of the post-petition loan agreement.

On December 4, 1987, the bankruptcy court approved Jay Alix as the trustee for the debtor-in-possession. See 11 U.S.C. @ 1104. Heller and the unsecured creditors' committee had moved for Alix's appointment. Neither SCPI nor FSI opposed his appointment as trustee, although earlier they had rejected him as an examiner. Alix, the Creditors' Committee and another FSI creditor, Michigan Strategic Fund, objected to the Consent Financing Order. Alix claimed the terms of the agreement made it impossible to operate without being in default and that the agreement gave Heller too much control. The bankruptcy court conducted several hearings between December 21, 1987 and January 7, 1988.

The court then entered an order amending [*7] the Consent Financing Order

The amended order determined that Heller's claims under the pre-petition loan agreements were valid and not subject to any claims, set-offs or defenses of FSI. It also confirmed the super priority status of Heller's secured claims. See 11 U.S.C. @ 364. The amended order expressly provided, "all parties in interest in this Proceeding, or any further or future proceeding whether under [any provision of the bankruptcy laws], are forever barred from prosecuting any actions or filing any claims against [Heller] arising or related to the Financing Arrangements. . . ."

Finally on May 4, 1998, the court approved a plan offered by FSI's employees' union, United Distributive Workers Council 30, for the purchase of FSI's assets by Country Home Bakery, Inc.. SCPI, Sanders and Kreissl participated in the plan process and did not object to the plan. Under the plan, Heller was paid the full amount of its allowed claims.

In 1989, SCPI, Sanders, Kreissl and Sam J. Merigian, a shareholder of SCPI, n2 sued Heller, Butzel, Keidan, Simon, Myers & Graham, Heller's attorneys, John W. Butler, a partner in the Butzel firm, and Alix. The complaint contained

thirteen counts alleging, [*8] among other things, common law fraud, RICO violations, and securities law claims. The district court dismissed all of the claims as barred on res judicata grounds, based on the bankruptcy case of Fred Sanders, Inc. See In re Fred Sanders, Inc., Case No. 87-06979-B (Bkrtcy. E.D. Mich. May 1, 1988). n3 The court also held that Merigian failed to state a claim upon which relief may be granted. SCPI, Sanders and Kreissl appeal as to the dismissal of their claims against all defendants. Merigian appeals only from the dismissal of the securities claims against Heller.

----------Footnotes----------

n2 The court denied Merigian's attempt to gain class certification to represent all shareholders.

n3 SCPI, Sanders and Kreissl argue that this 12(b)(6) motion should have been treated as a motion for summary judgment because the court considered "attachments to the pleading" in the form of the bankruptcy orders. Under either of these motions the court would have been entitled to take judicial notice of the prior bankruptcy proceeding.

----------End Footnotes----------

I. [*9] The district court dismissed all of the claims by all of the plaintiffs on res judicata grounds. We review de novo

district court dismissals of cases on res judicata grounds. Gargallo v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 918 F.2d 658 (6th Cir. 1990).

Courts apply the doctrine of res judicata to promote the finality of judgments, which in turn increases certainty, discourages multiple litigation and conserves judicial resources. See Federated Department Stores v. Moitie, 452 U.S. 394, 69 L. Ed. 2d 103, 101 S. Ct. 2424 (1981). Res judicata should not be confused with collateral estoppel or issue preclusion. This latter doctrine only "precludes relitigation of issues of fact or law actually litigated and decided in a prior action between the same parties and necessary to the judgment, even if decided as part of a different claim or cause of action." Gargallo, 918 F.2d at 661. In contrast, res judicata, or claim preclusion, has four elements:

1. A final decision on the merits in the first action by a court of competent jurisdiction;

2. The second action involves the same parties, or their privies, as the first;

3. The [*10] second action raises an issue actually litigated or which should have been litigated in the first action;

4. An identity of the causes of action King v. South Cent. Bell Tel. & Tel. Co., 790 F.2d 524 (6th Cir. 1986); Westwood Chemical Co. v. Kulick, 656 F.2d 1224 (6th Cir. 1981).

Confirmation of a plan of reorganization constitutes a final judgment in bankruptcy proceedings. Stoll v. Gottlieb, 305 U.S. 165, 83 L. Ed. 104, 59 S. Ct. 134 (1938); In re Chattanooga Wholesale Antiques, Inc., 930 F.2d 458 (6th Cir. 1991); Miller v. Meinhard-Commercial Corp., 462 F.2d 358 (5th Cir. 1972); see also 11 U.S.C. @ 1141(a) (outlining preclusive effect of confirmed plan). The bankruptcy court issued an order confirming a bankruptcy plan in the FSI bankruptcy in 1988, constituting a final judgment on the merits by a court of competent jurisdiction.

SCPI, Sanders and Kreissl contend that none of the other elements of res judicata has been met as to their claims. They argue that they were not a party, or in privity with a party in the bankruptcy for res judicata purposes. They assert that the only party [*11] to the FSI bankruptcy for res judicata purposes was the debtor FSI and that, while SCPI owned FSI, the two retained separate corporate identities and SCPI could not be considered a party to the bankruptcy.

We believe this definition of party and privies narrows the effect of a bankruptcy order too far. Other entities, such as

creditors and equity security holders in the debtor, must also be considered parties for res judicata purposes. The Bankruptcy Code contains a strong preference for final resolution of all claims involving the debtor, largely in order for the debtor to obtain a fresh start. Oneida Motor Freight, Inc. v. United Jersey Bank, 848 F.2d 414 (3rd Cir.), cert. denied, 488 U.S. 967, 102 L. Ed. 2d 532, 109 S. Ct. 495 (1988). To release creditors and equity security holders from the bonds of res judicata would allow them to launch collateral attacks on confirmed plans, undermining the necessary ability of bankruptcy courts to settle all of the claims against the debtor. To interpret the term "party" narrowly would also run counter to the provisions in the Code which outline the effect of plans and offer methods for challenging the bankruptcy orders. [*12] See, e.g., 11 U.S.C. @@ 1141,1144.

SCPI, Sanders and Kreissl all fit within an expanded definition of party. SCPI owned one hundred percent of the stock in FSI. In fact, FSI was SCPI's sole asset. Sanders filed a claim in the bankruptcy proceeding as a creditor. Both Sanders and Kreissl acted as personal guarantors of the Heller loan, making them both creditors of FSI as well. In re Justice Oaks II, Ltd., 898 F.2d 1544, 1551 (11th Cir.), cert.

denied 112 L. Ed. 2d 398, 111 S. Ct. 387 (1990). Similarly, Heller, Butzel and Butler would all qualify as parties to the bankruptcy because of their claims as creditors. Likewise, Alix as trustee for FSI is certainly a party to the proceeding.

The shareholder in SCPI, Merigian enjoyed a more distant relationship with FSI. He was neither an equity security holder in FSI, nor a creditor. Any relation he had to the FSI bankruptcy was through SCPI. Consequently, Merigian could not be considered to be a direct party to the proceeding.

Res judicata also bars those in privity with parties from bringing suit later. Privity in this sense means a successor in interest to the party, one who controlled the earlier action, [*13] or one whose interests were adequately represented. Latham v. Wells Fargo Bank, N.A., 896 F.2d 979 (5th Cir. 1990). Sanders was the chairperson of the boards of both FSI and SCPI; Kreissl was president of both companies. These positions of power allowed them to control the actions of FSI and SCPI. See In re Teltronics Services, Inc., 762 F.2d 185 (2nd Cir. 1985).

The district court found Merigian to have been in privity with SCPI because his interests were adequately represented by SCPI. The adequacy of representation is a factual matter for the district court. King v. South Cent. Bell Tel. & Tel. Co., 790

F.2d 524, 530 (6th Cir. 1986)(adequacy of representation in class action). Relying on Amalgamated Sugar Co. v. NL Industries, Inc., 825 F.2d 634 (2nd Cir.), cert. denied sub nom. Rothenberg v. Amalgamated Sugar Co., 484 U.S. 992, 98 L. Ed. 2d 511, 108 S. Ct. 511 (1987), the district court held that "the board of directors of SCPI owed a fiduciary duty to represent Merigian and the other shareholders and, absent bad faith, collusion, or negligence by the board, the stockholder is deemed adequately represented." [*14] The district court made no other factual examition of the adequacy of representation.

In Amalgamated Sugar, one shareholder in NL Industries brought an action in state court for a declaration of the validity of a "poison pill" stock purchase plan. A few weeks earlier the same plan had been challenged by Amalgamated Sugar and two other companies in an action brought against NL Industries and its directors in federal court. The federal court entered a consent judgment permanently enjoining implementation of the stock plan, and a few days later the court also enjoined the state proceedings. The Second Circuit upheld the injunction on res judicata grounds, but only after noting that "a finding of privity between a shareholder and the corporation depends on whether, under the

circumstances, the interests of the nonparty were adequately represented." Amalgamated Sugar, 825 F.2d at 640. NL Industries adequately represented the interests of the shareholder because he had no interest in the plan different from the directors. Id. at 641.

In this case, the district court failed to inquire into the particular circumstances of the case, and chose [*15] instead to apply a "bright line rule" for representation. This was error. Merigian's claims against Heller do not correspond with those of SCPI. Merigian argues that Heller as the control person of SCPI failed to make the necessary disclosures in relation to the issuance of SCPI stock. Only Merigian as a stockholder, not SCPI, could make this claim. Therefore, SCPI could not adequately represent Merigian's interests against Heller under this theory, and the FSI bankruptcy does not bar this action by Merigian.

The third element of res judicata prohibits parties from bringing claims they have already brought or should have brought. SCPI, Sanders and Kreissl first contend that their lender liability claims could not have been brought in the bankruptcy court because the court would have lacked subject matter jurisdiction. See 28 U.S.C. @@ 157, 1334. They believe that because bankruptcy courts only have

subject matter jurisdiction over core proceedings, a final judgment by a bankruptcy court is res judicata only as to core proceedings.

Three courts of appeals have considered this argument. Both the Fifth and the Seventh Circuits have held that decisions in bankruptcy cases [*16] act as a bar only to core proceedings. Barnett v. Stern, 909 F.2d 973 (7th Cir. 1990); Howell Hydrocarbons, Inc. v. Adams, 897 F.2d 183 (5th Cir. 1990). More recently, the Second Circuit held that whether or not a claim was a core proceeding had no bearing on its preclusion. Sure-Snap Corp. v. State St. Bank and Trust Co., 948 F.2d 869 (2nd Cir. 1991). We agree with the Second Circuit that in certain circumstances bankruptcy proceedings can also be binding on non-core proceedings.

The jurisdiction of federal district courts in bankruptcy matters is set out at 28 U.S.C. @ 1334:

Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

28 U.S.C. @ 1334(b); see also, 28 U.S.C. @ 1334(a) (granting jurisdiction over the bankruptcy petition itself). To

fall within the bankruptcy jurisdiction of a district court, a proceeding need only be "related to" a case under title 11. In re Wolverine Radio Co., 930 F.2d 1132, 1142 (6th Cir. 1991). [*17] A matter is related to a bankruptcy case if "the outcome of that proceeding could conceivably have any effect on the estate being administered in bankruptcy." Id., quoting In re Pacor, Inc., 743 F.2d 984, 994 (3rd Cir. 1984)(emphasis omitted). The matter need not directly involve the debtor, as long as it "could alter the debtor's rights [or] liabilities," but an "extremely tenuous connection" will not suffice. In re Wolverine Radio, 930 F.2d at 1142.

The claims brought by SCPI, Sanders and Kreissl would all qualify as proceedings "related to" the FSI chapter 11 case. They based their lender liability, securities fraud, RICO, bankruptcy fraud, and conspiracy claims against the Heller defendants and the bankruptcy trustee Alix on the same facts the bankruptcy court considered in determining the validity of Heller's secured claim against the FSI bankruptcy estate. Heller's claim, unlike those of other FSI creditors, was fully paid. Consequently, a successful action on the SCPI plaintiffs' part could have affected the outcome of the bankruptcy proceeding by calling into question the validity of Heller's claim and possibly resulted in the removal [*18] of

Alix as the trustee. Thus, despite the absence of FSI as a formal party to this action, these claims would have been within the district court's subject matter jurisdiction over bankruptcy cases.

If a district court has bankruptcy jurisdiction over a case, 28 U.S.C. @ 157(a) allows the court to refer the case to the bankruptcy court. 28 U.S.C. @ 157(a). Bankruptcy judges "may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11 . . . and may enter appropriate orders and judgments. . . ." 28 U.S.C. @ 157(b)(1).

The bankruptcy judge rules on whether a particular proceeding is a core proceeding. 28 U.S.C. @ 157(b)(3). The court looks at both the form and the substance of the proceeding in making its determination. In re Wolverine Radio, 930 F.2d at 144; In re Wood, 825 F.2d 90 (5th Cir. 1987). A core proceeding either invokes a substantive right created by federal bankruptcy law or one which could not exist outside of the bankruptcy. Id. In non-core proceedings that are "related to" the bankruptcy case, the bankruptcy judge may hear the matter and "submit proposed [*19] findings of fact and conclusions of law to the district court,"

but without the parties consent the bankruptcy court may not make a final decision on the matter. 28 U.S.C. @ 157(c)

Although the bankruptcy court would not have subject matter jurisdiction over a non-core related proceeding, the action would still be within the district court's jurisdiction. The Fifth and Seventh Circuits overlooked this ability of the district court to issue a necessary decision in a related matter in their decisions that res judicata bars only core proceedings. See Barnett v. Stern, 909 F.2d 973 (7th Cir. 1990); Howell Hydrocarbons, Inc. v. Adams, 897 F.2d 183 (5th Cir. 1990). While the bankruptcy court could not make a final decision in a non-core proceeding, absent the consent of the parties, it could hear the matter and refer it to the district court. Through its bankruptcy jurisdiction, the district court could decide the claim, allowing for a correct adjustment of the relations between all of the parties. Therefore, a confirmed plan in a bankruptcy case may operate to bar both core and non-core proceedings. n4

----------Footnotes----------##

n4 The SCPI plaintiffs never submitted this claim to the bankruptcy court, so the bankruptcy judge never determined whether they constituted core proceedings. The district court

in this case, however, did hold that the claims were core proceedings:

> claims challenging the conduct of the trustee in the administration of the estate, challenging the validity of Heller's pre-petition claims against the estate, Heller's conduct as post-petition lender pursuant to the consent financing orders, the propriety of liquidation versus reorganization of the debtor and allegation of fraud on the bankruptcy court . . . are all core proceedings. . .

The district court then alluded to the jurisdiction of bankruptcy court over non-core proceedings, but failed to mention which proceedings were non-core and to note the limited nature of the bankruptcy court's jurisdiction in these matters.

None of SCPI, Sanders or Kreissl's claims could be considered to "arise under title 11" because the causes of action are not created or determined by a statutory provision of title 11. See In re Wolverine Radio, 930 F.2d at 144. Likewise, the lender liability, common law fraud, securities fraud, and RICO claims against Heller, Butler and Butzel are not ones which "arise in" a title 11 case because they could arise in cases other than bankruptcy proceedings. See id. Therefore, despite their possible affect on the bankruptcy

estate of FSI, the district court incorrectly classified them as core proceedings rather than as non-core related proceedings.

The claims against the trustee Alix, however, would be core proceedings. While the specific causes of action, such as RICO, exist independently of bankruptcy cases, an action against a bankruptcy trustee for the trustee's administration of the bankruptcy estate could not. All claims against Alix related to his conduct during the FSI bankruptcy, and should be considered core proceedings.

----------End Footnotes----------

[*20] The SCPI plaintiffs next argue that they could not have brought their claims in the bankruptcy proceeding because the claims did not involve the debtor. Generally, bankruptcy jurisdiction does not extend to actions between third parties because the action would not be "related to" a bankruptcy proceeding. For example, a bankruptcy court would not hear a case between two creditors based on their prior dealings independent of the debtor. In contrast, as detailed above, if this case had been brought during the bankruptcy proceedings it would have affected the bankruptcy estate. Therefore, the SCPI plaintiffs could have brought this action

in the prior proceeding, and have offered no justification for their failure to do so.

Res judicata also requires an identity of claims. SCPI, Sanders and Kreissl incorrectly contend that because these particular claims were not raised in the prior action, no identity of claims exists. Identity of causes of action means an "identity of the facts creating the right of action and of the evidence necessary to sustain each action." Westwood Chemical Co. v. Kulick, 656 F.2d 1224, 1227 (6th Cir. 1981). All of the claims in this action [*21] are based on Heller's behavior in making and administering its loan to FSI. The bankruptcy considered this same behavior by Heller in its numerous rulings on the validity of Heller's claims against FSI. Therefore, these claims are identical and all of the elements of res judicata have been met.

SCPI, Sanders and Kreissl make one final argument supporting their action. They insist that only compulsory counterclaims are barred by res judicata. n5 See Bankr. R. 7013; Fed. R. Civ. P. 13. SCPI's bases this argument largely on a Fifth Circuit case, D-1 Enterprises, Inc. v. Commercial State Bank, 864 F.2d 36 (5th Cir. 1989). In D-1 Enterprises, the court of appeals allowed a debtor to bring a lender liability action after the district court entered an agreed order lifting

the automatic stay and abandoning the debtor's property to the lender. The court's decision rested largely on the limited nature of the automatic stay proceedings. Id. at 38-39. The summary nature of the proceedings was inappropriate for dealing with "indirect defenses" such as fraud. The court found additional support for its position in the compulsory counterclaim [*22] provisions of the Code, finding that "it would be odd indeed if a claim that was not required as a compulsory counterclaim by the Bankruptcy Rules and in fact could not be litigated as a defense to the motion for relief from the stay was nonetheless barred by res judicata." Id. at 39. Thus, the ruling in D-1 Enterprises rested largely on the limited nature of the proceedings to lift the automatic stay, not on whether a particular claim was a compulsory counterclaim.

----------Footnotes----------

n5 Since these claims arise from the same core of operative facts as the bankruptcy, they would be considered compulsory counterclaims.

----------End Footnotes----------

Subsequent cases in the Fifth Circuit support this interpretation of D-1 Enterprises. In its recent decision in In re Howe (Howe v. Vaughan), 913 F.2d 1138 (5th Cir. 1990), the

court stated, "the D-1 Enterprises court merely decided that when a claim cannot be litigated effectively, it is not precluded." Howe, 913 F.2d at 1146; see also [*23] , Hendrick v. Avent, 891 F.2d 583 (5th Cir.), cert. denied 112 L. Ed. 2d 39, 111 S. Ct. 64 (1990) (distinguishing D-1 Enterprises from Southmark Properties v. Charles House Corp., 742 F.2d 862 (5th Cir. 1984) on the basis of the limited nature of the proceeding in D-1 Enterprises). In Howe, the debtors had listed their lender as a creditor and had the opportunity to be heard in the proceedings. This prompted the court to hold "that when a confirmed plan discloses and specifically treats the creditor's claim in an adversary proceeding that is, in effect, settled in the plan, the debtor cannot collaterally attack the bankruptcy court's decision five years later in an action based on the same transaction." Howe, 913 F.2d at 1147; see also Southmark Properties v. Charles House Corp., 742 F.2d 862 (5th Cir. 1984) (President and 25% stockholder of the debtor (Craig) cannot bring lender liability claim against creditor three years after final sale in Chapter X bankruptcy).

As these cases point out, what is important is not whether a particular claim is compulsory, but whether the claim should [*24] have been considered during the prior action. A

number of adversary proceedings, culminating in an order confirming a reorganization plan, determined the rights of the parties to the FSI bankruptcy. The court conducted these proceedings to resolve all of the claims currently owed by the debtor in order to discharge its debts. The confirmation order resulted in a plan paying Heller's claim against the estate in full as an unimpaired secured creditor. The claim asserted by SCPI, that Heller obtained its favored position through illegal practices, runs counter to the bankruptcy court's determination. Accordingly, these claims of SCPI, Sanders and Kreissl should have been brought during the bankruptcy proceeding, and res judicata prevents them from being raised now.

III. The district court dismissed Merigian's securities claims for failure to state a claim for which relief could be granted. See Fed. R. Civ. P. 12(b)(6). The court held that Heller, being neither a seller nor an active participant in the offering, owed no duty to disclose to the purchasers of SCPI stock, and so could not be held liable under either section 12(2) of the Securities Act of 1933, 15 U.S.C. @ 77l, [*25] or section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934, 15 U.S.C. @ 78j(b); 17 C.F.R. 240.10b-5. "[A] complaint should not be dismissed for failure to state a claim unless it

appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." Conley v. Gibson, 355 U.S. 41, 45-6, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957). We review de novo dismissals under Rule 12(b)(6). Craighead v. E.F. Hutton & Co., 899 F.2d 485, 489 (6th Cir. 1990).

Merigian argues, however, that the district court's holding ignored Heller's potential liability as a "controlling person" of SCPI, see 15 U.S.C. @@ 77o, 78t, and this claim forms the crucial argument in his appeal. A "controlling person" shares the liability for violations of securities laws with the primary violator it controlled. Id. If Heller controlled SCPI and SCPI violated its duty to disclose, then Heller could also be held liable as a "controlling person." Additionally, Merigian claims the court neglected to consider Heller's liability for "aiding and abetting" SCPI's violation of section 10(b) and Rule 10b-5.

Heller contends the district court did [*26] not ignore these potentialavenues of liability, but rather Merigian failed to adequately plead any of these causes of action. Since Heller did not offer or sell SCPI stock, section 12(2) could not apply to it unless it "controlled" SCPI. See 15 U.S.C. 77l. Byholding that Heller was not an offerer or seller, the district court

implied that Merigian had failed to plead sufficiently Heller's control over SCPI. According to Heller, Merigian failed either to allege any control relationship between Heller and SCPI or to allege sufficient acts of control over SCPI by Heller to make it a "controlling person."

The 78 page amended complaint does not contain a specific allegation of control over SCPI by Heller. In two paragraphs, Merigian contends that the financing agreement between FSI and Heller gave Heller control over FSI. Of Course, SCPI, not FSI, sold the stock in question. Merigian claims that these references to Heller's control over FSI are essentially typographical errors. The complaint really should be read as stating that the loan agreements with FSI gave Heller control over SCPI. Merigian argues this reading becomes apparent upon examination of the remainder of the complaint. [*27] Merigian points to a number of paragraphs which simply assert Heller's status as a control person, and continue to allege violations of the securities laws by SCPI. Contrary to Merigian's assertions, these paragraphs do not support a conclusion that the earlier paragraphs mistakenly alleged control over FSI rather than SCPI. At best, the complaint could be read as implying that control over FSI equalled control over SCPI. n6 A generous

reading of the complaint, we believe, suffices to adequately allege Heller's status as a control person under section 15 of the 1933 Act, 15 U.S.C. @ 77o.

- - - - - - - - - - - - - - - - - -Footnotes- - - - - - - - - - - - - - - - - -##

n6 This implication of control would be consistent with our finding that SCPI's actions here are barred by res judicata.

- - - - - - - - - - - - - - - - - -End Footnotes- - - - - - - - - - - - - - - -

Where Merigian's complaint fails is in its allegations of a control relationship. While normally Heller's status as a control person would be a question of fact, the allegations of the complaint here are unusually explicit and enable us to conclude as a matter of law that as to Merigian, Heller was not such a [*28] control person and further that Merigian, even if allowed to amend, could not plead or prove sufficient facts to support a contrary conclusion or raise a factual issue concerning it.

Our circuit has not adopted a test for liability as a "controlling person" under the securities laws, although other circuits have considered the issue, with slightly conflicting results. See, e.g., Orloff v. Allman, 819 F.2d 904, 906 (9th Cir. 1987); Metge v. Baehler, 762 F.2d 621 (8th Cir. 1985), cert.denied, 474 U.S. 1057, 106 S. Ct. 798, 88 L. Ed. 2d 774 (1986). We find it unnecessary to choose between the

various tests suggested because Merigian failed to plead sufficient acts of control under the least rigorous standard applied in Metge.

Metge established a two-prong test for control person liability. The plaintiff needs to establish "that the defendant lender actually participated in (i.e., exercised control over) the operations of the [borrower/violator] in general . . . [and] that the defendant possessed the power to control the specific transaction or activity upon which the primary violation is predicated." Metge, 762 F.2d at 631. In [*29] Metge, the lender alleged to occupy a control person role had acquired substantial additional powers beyond a simple security interest in property. The lender held nearly 20% of the borrower's stock, held a proxy on a controlling interest of the borrower's subsidiary, had power over the borrower's policy regarding capital stock, bank personnel attended board meetings, and it influenced the borrower's debt structure. Metge at 631. Despite all of this power, the Eighth Circuit held that the facts suggested only the potential for control, not actual control. Metge at 632.

Similarly, Merigian only alleged participation in the specific activity without attempting to establish broader actual control. The complaint states that Heller participated in the

development of the prospectus by complying with SCPI's due diligence requirement and making disclosures concerning the FSI loan and that Heller "controlled" the information it gave to SCPI. Nowhere does Merigian claim that Heller "actually participated in the operations" of SCPI, other than by making secured loans. Extending a loan to a company and taking measures to secure that loan do not amount to actual control. Schlifke v. Seafirst Corp., 866 F.2d 935, 949 (7th Cir. 1989). [*30] Therefore, Merigian's complaint failed to make out a claim under either of the "controlling person" statutes, 15 U.S.C. @@ 77o, 78t.

The district court also found correctly that Merigian's complaint failed to make out a claim for aiding and abetting liability under section 10(b) and Rule 10b-5 against Heller. A claim of aiding and abetting under these sections requires allegations that the accused party knowingl and substantially assisted another party's violation of the securities law, and that the accused had a general awareness that it was participating in an overall improper activity. Moore v. Fenex, Inc., 809 F.2d 297 (6th Cir.), cert. denied, 483 U.S. 1006, 107 S. Ct. 3231, 97 L. Ed. 2d 737 (1987). Thus, Heller could be held liable as an aider and abettor only if SCPI violated section 10(b).

Merigian failed, however, to allege adequately SCPI's commission of a violation of section 10(b) and Rule 10b-5. Generally, damage claims under this section and rule require "1) the use of jurisdictional means 2) to implement a deceptive or manipulative practice (with the requisite scienter) 3) in connection with 4) the purchase or sale of 5) a security 6) causing 7) damages." Craighead v. E.F. Hutton & Co., 899 F.2d 485 (6th Cir. 1990) [*31] quoting Mansbach v. Prescott, Bali & Turben, 598 F.2d 1017, 1026 (6th Cir. 1979). Here, Merigian failed to allege that SCPI acted with scienter, "an intent to deceive, manipulate or defraud." See Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193, 47 L. Ed. 2d 668, 96 S. Ct. 1375 (1976). Instead, Merigian claims that SCPI did not know of Heller's "scheme" to deny funding and send SCPI into bankruptcy. Therefore, SCPI could not have acted intentionally when it failed to reveal the information about Heller's plans for its future, and so SCPI lacked the requisite scienter to be guilty of a section 10(b)/Rule 10b-5 violation. Consequently, Heller could not be liable under a secondary theory of liability regardless of its level of knowledge.

The failure to establish Heller's status as a control person also destroys the shareholder's RICO claims. RICO contains

a proximate cause requirement. Holmes v. Securities Investor Protection Corp., 117 L. Ed. 2d 532, 112 S. Ct. 1311 (1992). The district court found this to be lacking because a shareholder does not suffer a direct personal injury when the damage alleged is diminution or destruction of the value of the stock. Gaff v. FDIC, 814 F.2d 311 (6th Cir. 1987); [*32] Warren v. Manufacturer's Nat'l Bank, 759 F.2d 542 (6th Cir.1985). When the acts alleged lower the corporation's value, the corporation suffers the direct injury, and the shareholders suffer as a result because their investment is worth less. The bankruptcy fraud alleged also constitutes such an indirect injury. As the Supreme Court recently explained, "a plaintiff who complains of harm flowing merely from the misfortunes visited upon a third person by the defendant's acts [generally stands] at too remote a distance to recover." Holmes at 1318.

Merigian alleged (insufficiently however) an additional act beyond the mere diminution of the stock's value. He also claimed that Heller through SCPI failed to disclose material facts in an issuing prospectus. Relying on the false prospectus, Merigian bought valueless stock. Thus, in the abstract, this second act of issuing a misleading prospectus could have proximately caused Merigian's injury.

Where Merigian's complaint goes awry, however, is in the establishment of the necessary predicate acts. 18 U.S.C. @ 1961(5) requires at least two predicate acts underlying RICO claims. Merigian alleged four: securities fraud, [*33] bankruptcy fraud, and mail and wire fraud in the perpetration of the other two acts. As we explained above, Heller could not be held liable for violations of the securities laws by SCPI. Furthermore, the claimed acts of bankruptcy fraud did not proximately cause injury to Merigian as forcing a company into bankruptcy directly injures only the company. Likewise, the mail and wire fraud claims could not support a RICO action because they are based on the securities and bankruptcy fraud claims we just found inadequate to support a RICO action, and offer no closer connection to any of the parties than the substantive claims did. Therefore, lacking any predicate acts on which to base the RICO claim, the district court's dismissal of the RICO claim was also proper.IV.

For the foregoing reasons, we AFFIRM the district court's dismissal of the claims against Heller, Butzel, Keidan, Simon, Myers & Graham, John Butler, Jr. and Jay Alix.

APPENDIX -2

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

SANDERS CONFECTIONERY
PRODUCTS, INC., et. al.,

C.A. No. 89-CV-60028-AA

Plaintiffs,

HON. GEORGE La PLATA

vs.

HELLER FINANCIAL, INC., et. al.,

Defendants.

_____/

MEMORANDUM OPINION AND ORDER OF DISMISSAL

OPINION

Plaintiffs brought this action February 6, 1989, and filed a first amended complaint (1AC) in May 1989, against the defendants which alleges thirteen counts, including common law fraud, fraud on the bankruptcy court, misrepresentation, breach of the duty of good faith, unfair business practice, abusive control, securities fraud, conspiracy, class action of shareholders, RICO claims, and negligent, reckless or bad faith handling of financial arrangements. The case is currently

pending on overlapping motions to dismiss by the defenda and a motion to amend the 1AC filed by a shareho plaintiff.

The plaintiffs are Sanders Confectionery Products, (SCPI), a Michigan corporation, parent company and s common stockholder of Fred Sanders, Inc. (FSI) (the Deb in the related bankruptcy case); Mr. John Sanders, Chairm of both SCPI and Sanders, Inc.; Mr. Filipp Kreissl, President both SCPI and Sanders, Inc.; and Mr. Sam Merigian, himself and all other shareholders of SCPI. The defenda are Heller Financial, Inc., a secured creditor and post petiti lender of the debtor FSI; Butzel, Keidan, Simon, Myers a Graham (Butzel), attorneys for Heller; and John W. Butler partner in the Butzel firm. These defendants, aligned togeth and represented by the same counsel, will be referred to as t Heller defendants. Finally, the last defendant is Jay Alix, t trustee in bankruptcy for the Debtor FSI. FSI which became subsidiary of SCPI in July 1986 is not a party to this action.

The Heller defendants and Mr. Alix brought separa motions to dismiss the complaint which were made moot the filing of the 1AC. They then filed motions to dismiss t 1AC and plaintiff Merigian filed a motion for leave to ame the 1AC. The Court granted the requests for oral argument

the pending motions, which was held on July 27, 1990.

Both Alix and the Heller defendants argue that this action must be dismissed as it is an impermissible collateral attack on the orders of the bankruptcy court in the Chapter 11 proceeding In re Fred Sanders, Inc. On a motion to dismiss for failure to state a claim, the Court must accept the plaintiffs allegations as true. Fed. R. Civ. P. 12(b)(6), Hishon v. King & Spaulding, 104 S. Ct. 2229, 2232 (1984). Rule 12(b)(6) authorizes a court to dismiss a claim on the basis of a dispositive issue of law, and a claim must be dismissed if, as a matter of law, it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations. Id, citing Conley v. Gibson, 355 U.S. 41, 45-46 (1957). Accord, Neitze v. Williams, 109 S.Ct. 1827, 1832 (1989). The court may consider the allegations of the complaint, the exhibits to th complaint and the public record from the bankruptcy proceeding. Wright & Miller, Fed. Practice & Procedure, 1357.

Under res judicata, also known as claim preclusion, a final judgment on the merits bars a later action by the same parties on the same causes of action, including claims which could have been but were not litigated. Consol. TV Cable v. City of Frankfort, 857 F.2d 354 (6th Cir. 1988), cert den 109 S.

Ct. 1537 (1989). It is well settled that an order confirming a plan of reorganization is a final judgment for res judicata purposes. Stoll v. Gottlieb, 305 U.S. 165 (1938). Under the federal rule of res judicata applicable here, "cause of action" is defined as a core or nucleus of operative facts, a transaction, or a series of transactions. Matter of Energy Co-Op, Inc., 814 F.2d 1226 (7th Cir. 1987), cert den 484 U.S. 928 (1987) (not same evidence test).

The identity of parties element may be satisfied not only where there are the same formal parties, but also where a party's interests are adequately represented by someone in the prior action. In bankruptcy, one who participates in a Chapter 11 proceeding, becomes party to that proceeding even if never formally named a party. Republic Supply Co v. Shoaf, 815 F2d 1046 (5th Cir. 1987), In re Met-L-Wood Corp., 861 F.2d 1012 (7th

Cir. 1988), cert den 109 S.Ct. 1642 (1989), In re Justice Oaks, II, 898 F.2d 1544 (11th Cir. 1990), notwithstanding Martin v. Wilks, 109 S. Ct. 2180, n 2 (1989).

Parties in interest, who have the right to appear and be heard on any issue in a case under Chapter 11, specifically include creditors and equity security holders. 11 U.S.C. 1109(b). Guarantors of a debtor are creditors having a claim

against the debtor, albeit contingent. Justice Oaks II. An equity security holder means holder of equity security of the debtor, including a share in a corporation, or interest in limited partnership. 11 U.S.C. 101 (15) and (16). A confirmed plan of reorganization binds the debtor as well as any creditor or equity security holder in the debtor, whether or not its interest is impaired and whether or not it accepts the plan. 11 U.S.C. 1141(a). In addition, only a party can file a plan. 11 U.S.C. 1121.

Having carefully reviewed the record, the extensive briefs and the applicable law, and having heard argument on the motions, this Court concludes as follows:

The Court summarizes the factual basis for the claims from the 457 paragraph, 78 page 1AC and the orders of the bankruptcy court. (1) The 1AC alleges that FSI, under Chapter 11

---

(1) Defendant Alix seeks dismissal under Fed. R. Civ. P. 8 and 12(f), on the grounds that the complaint is not as short, plain or concise as is reasonable under the circumstances; improperly recites lengthy evidentiary material; and contains redundant, inflammatory and scandalous allegations. While the Court agrees that the 1AC is lengthy and burdensome to

the Court and the defendants, the motins to dismiss should be considered on the merits rather than having another complaint filed. protection between 1981 and 1983, had showed declining losses from 1981 to 1985, and in 1985 had decided to try to grow. Kreissl approached Heller for financing and a discussed need for two levels of funding, a $2.45 million line of credit and, beyond that, "mezzanine funding" and equity participation by Heller. In late 1985, they negotiated financing and, based on FSI's understanding of the financing, FSI began investing heavily in January, 1986. Plaintiffs allege that Heller did not disclose to FSI that the Michigan office of Heller only had lending authority of $2.5 million and anything more would have to get approval from the Chicago office. Although the borrowing formula in the Loan Agreement sent to FSI in February 1986, would reduce the amount of the cash advance to below FSI's expectations, it was signed. The Loan was funded in March 1986. FSI continued to request that Heller adjust the formula. The refusal to do so allegedly caused "under funding," the shortfall of cash in December 1986, and precipitated new financial problems for FSI. Plaintiffs also allege that Heller failed to disclose its own financial losses for 1985 to FSI and that if known, would have sought financing elsewhere. In July 1986, Heller declared Events of Default,

accelerated the loan and stopped all funding. As a requirement for cure of the defaults, Heller (through Mr. Butler) demanded that FSI execute a First Amendment to the Loan Agreement which included new terms substantially favorable to Heller. These terms included: Loan Guarantees by SCPI, Sanders and Kreissl; the release of cure period rights and all claims against Heller; acceptance of a "blocked account" for all cash collections; and an interest rate increase. Meanwhile, Heller continued to refuse to change the borrowing formula and only after the Amendment was signed would Heller advance money to start building Christmas inventories. An advance of $300,000.00 was made on the guarantee of the Union of FSI employees. SCPI was preparing a public stock offering for early 1987, and on December 9, 1986, Heller certified to the attorneys for SCPI that FSI was a borrower in good standing. But then in a December 31st letter, Heller claimed defaults of state and federal taxes, which Heller says it did not discover until December 19th. Plaintiffs allege that the defaults were cured by FSI, but to avoid revision of the offering prospectus FSI asked for a waiver and estoppel letter from Heller. Heller would not execute this letter without FSI entering an "Interim Operational Letter AGreement" which gave Heller further

powers.

On January 26, 1987, a Second Amendment to Loan Agreement extended the maturity date on the $300,000 loan, on the personal guarantees of Sanders and Kreissl. Plaintiffs allege that had Heller honored its original commitment, the taxes would have been paid, the alleged defaults would not have occurred and the Second Amendment would not have been necessary. In February 1987, still refusing to change the borrowing formula, Heller orally agreed to loan an additional $750,000 if the public offering raised at least $1 million. Plaintiffs allege this loan was never made, although the stock offering completed in May, 1987, raised $5 million.

In February 1987, Heller declared defaults with respect to taxes, some required financial disclosures, and the $300,000 loan due on February 16. FSI met the conditions of cure. In May, FSI learned in confidence that Heller's Michigan office would close. When FSI got loan approval for $600,000 from First Independence relying on the stock offering, Heller cooperated. But, at execution of the loan, Heller more than doubled its demand for payment out of the loan to $120,000 and accelerated the maturity date of its loan by eight months. In August 1987, the state issued another tax lien in error, First Independence and Heller declared defaults, which were

ultimately rescinded. After Heller's Michigan office closed, Heller informed FSI that it's plans did not include small business loans. With the defaults declared in September, Heller told FSI to find new financing. Heller had denied FSI a Christmas inventory loan for 1987, but when FSI still needed money in October, Heller made additional loans.

FSI prepared a $1 million debt offering for September or October 1987, but it was delayed because of the stock market crash. On November 5, 1987, Heller sent letter of default stating it would only continue stop-gap financing at its sole and absolute discretion, on day to day basis. At a November 9th meeting, FSI asked for $450,000 to meet Christmas sales needs and Heller promised to do everything it could to get it. But, instead, Heller failed to show at a meeting set for November 13th and filed an action for reclamation to foreclose on the loans.

On November 14th, Heller demanded that FSI file for Chapter 11 protection and execute a new loan agreement for the funds needed to meet payroll. Plaintiffs allege that the new agreement was not negotiated for, was not drafted in good faith and did not disclose Heller's intention to prevent the rehabilitation of FSI. On November 16th, FSI filed its Chapter 11 petition and the next day requested the appointment of an

examiner. Of the names on the list, only Jay Alix was rejected by FSI because of his contacts with Kreissl in prior business dealings, which apparently led to litigation between them.

On November 18th, the Debtor filed a motion for authorization to borrow additional funds from Heller, as other sources of financing could not be found. A Post-Petition Loan and Security Agreement provided for discretionary financing to the Debtor and waiver by the Debtor, SCPI, Sanders and Kreissl of all claims, set-offs or defenses to Heller's rights as a creditor, or which contested the conduct of Heller in administering the financing agreements. After hearing, the Bankruptcy Court entered the Consent Financing Order which approved and incorporated by reference the Post-Petition Agreement and ratified the terms of the Pre-Petition Agreements. Although SCPI, Sanders and Kreissl did not sign the Consent Order itself, they were party to and guarantors under the Post-Petition Loan Agreement which was incorporated into the Consent Order.

Plaintiffs allege that on December 4, 1987, Heller gave FSI an ultimatum that Alix be appointed trustee or else all funds would be cut off. Alix failed to disclose any prior contact with FSI or the animosity between he and Kreissl. On the motion of Heller and the unsecured creditors' committee, the

Bankruptcy Court appointed Alix the Chapter 11 operating trustee for the debtor-in-possession. Neither SCPI nor FSI, both represented by Sanders and Kreissl, opposed the appointment of Alix even though they had allegedly rejected him as an examiner. Plaintiffs do not allege that Alix was involved in the relationship between Heller and FSI before his appointment in December 1987.

The Creditors' Committee, the Michigan Strategic Fund and Jay Alix objected to the Consent Financing Order and Alix sought other financing. Alix objected to the terms of the financing agreement as impossible to operate under without being in default and as giving the Lender too much control. There were further negotiations and several hearings before the Bankruptcy Court between December 21, 1987, and January 7, 1988, when the Court entered a "Supplemental Consent Financing Order Amending and Confirming Initial Financing and Adequate Protection Order."

This Supplemental Consent Financing Order determined that Heller's claims under the Loan Agreement were valid and not subject to any claims, set-offs or defenses by the Debtor. It also confirmed the super-priority status of Heller's secured claims. The Supplemental Order expressly provided that all parties in interest in this proceeding or any

other bankruptcy proceeding are forever barred from prosecuting any action or filing any claims against Heller arising from or related to the Financing Arrangements, para.8. It also stated that provisions of the Order are binding on all parties in interest to the proceeding and that the Order is a final order deemed to be res judicata on all terms and provisions, para.7.

According to the Supplemental Consent Order, the Debtor and Trustee would file a plan of Reorganization by March 1, 1988, and best efforts would be made to get confirmation of the plan by April 1, 1988. On March 1st, Alix filed a Trustee's Liquidating Plan of Reorganization which proposed the sale of substantially all the assets to a single purchaser. At the very latest, there could be no doubt at this point that Alix intended to liquidate the Debtor's assets.

Three plans were developed and approval given for a joint disclosure. The plans were (1) a reorganization plan by FSI and SCPI, which intended to restore the business to FSI and would not extinguish the equity of SCPI shareholders; (2) a plan offered by the Union (at the behest of Alix) for the purchase of the Debtor's assets by Country Home Bakery, Inc.; and (3) a plan offered by Alix for the purchase of the Debtor's assets by Elias Brothers Restaurants, Inc. The Joint Disclosure

Statement, signed by John Sanders in his capacity as chairman for both FSI and SCPI, described the relationship between FSI and Heller as cooperative. The FSI/SCPI plan was withdrawn for failure to deposit $500,000 in earnest money as required. At the confirmation hearing in April 1988, Alix represented that the Trustee/Elias Brothers plan would be withdrawn if the Union/Country Home plan was capable of being confirmed. On May 4, 1988, Judge Brody entered the "Order Confirming Third Amended Plan of Reorganization of the United Distributive Workers, Council 30," confirming the Union/Country Home plan which liquidated the Debtor. Although SCPI, Sanders and Kreissl did not sign this Order, they participated in the process, and did not object to the plan or its treatment of Heller.

The assets and the name "Fred Sanders" were sold pursuant to the Confirmation Order. There is no indication that any of the plaintiffs appealed the orders of the bankruptcy court or moved for modification of the Confirmation Order.

This Court finds from the allegations of the 1AC that this action arises from the same core of operative facts and the same transactions as in the bankruptcy case. SCPI, John Sanders and Filipp Kreissl could have challenged the alleged scheme of the Heller defendants to use the financial

arrangements to get control of FSI, force it into bankruptcy, and liquidate it for the purposes of recouping loans and avoiding lender and securities liability, as well as the actions taken for that alleged purpose. The claims arising from the alleged bad faith, strong-arm pre-petition conduct of the Heller defendants, culminating in the Chapter 11 petition, and appointment of Alix as trustee, could have been raised, and the validity of the debts to Heller challenged when litigated. Even the securities fraud claims challenge the financial arrangements and allege failure to disclose as part of the scheme. The post-petition conduct of all the defendants (including the alleged complicity of Alix), to control the bankruptcy proceeding, impede reorganization of the debtor and have it effectively liquidated, could have been raised.

The appointment of Alix could have been challenged from the beginning as adversarial. But certainly with the firing of Kreissl from FSI, the continued threats to stop funding, the Consent Orders entered, the trustee's March 1st liquidation plan, and alleged interference with reorganization plans, there was sufficient notice of the alleged scheme to have challenged Heller's pre-petition claims as resulting from fraud, breach of contract or bad faith control over FSI or to have objected to or tried to set aside the bankruptcy consent orders and

confirmation order. Instead, plaintiffs entered the SEcond Amended Loan Agreement and did not object as parties in interest to the consent orders waiving their rights or to the confirmation order liquidating the debtor and did not appeal from them. Miller v. Meinhard-Commercial Corp., 462 F.2d 358 (5th Cir. 1972. Met-L- Wood, supra.

Plaintiffs argue that the bankruptcy court lacks subject matter jurisdiction to hear the controversies in this case because the debtor is not a party to this case and the claims are not "core" proceedings. However, the bankruptcy judge has subject matter jurisdiction of claims challenging the conduct of the trustee in the administration of the estate, challenging the validity of Heller's pre-petition claims against the estate, Heller's conduct as post-petition lender pursuant to the consent financing orders, the propriety of liquidation versus reorganization of the debtor and allegations of fraud on the bankruptcy court because they are all core proceedings even though the debtor is not a party. Furthermore, there is subject matter jurisdiction of related non-core proceedings where the dispute has a material impact on the assets of the estate or its administration. Compare In re Kham, 97 B.R. 420 (N.D. Ill. 1989). In fact, these issues were litigated in the bankruptcy proceeding.

Plaintiffs SCPI, John Sanders and Filipp Kreissl participated in the bankruptcy proceeding and were parties for res judicata purposes. Also, as the equity security holder and as guarantors of the debtor's liabilities they were parties in interest, bound by the bankruptcy court orders. Therefore, this Court finds the claims of these plaintiffs are barred by res judicata. Hendrick v. Avent, 891 F.2d 583 (5th Cir. 1990).

Lastly, plaintiff Merigian, as a shareholder of SCPI, may be in privity with SCPI, and therefore his claims also barred by res judicata, if his interests were adequately represented. Amalgamated Sugar v. NL Industries, 825 F.2d 634 (2nd Cir. 1987). In this case, the board of directors of SCPI owed a fiduciary duty to represent Merigian and the other shareholders and, absent bad faith, collusion, or negligence by the board, the stockholder is deemed adequately represented. Id. Therefore, this Court finds the claims of these plaintiffs are barred by res judicata. Hendrick v. Avent, 891 F.2d 583 (5th Cir. 1990). Lastly, plaintiff Merigian, as a shareholder of SCPI, may be in privity with SCPI, and therefore his claims also barred by res judicata, if his interests were adequately represented. Amalgamated Sugar v. NL Industries, 825 F.2d 634 (2nd Cir. 1987). In this case, the board of directors of SCPI owed a fiduciary duty to represent Merigian and the

other shareholders and absent bad faith, collusion, or negligence by the board, the stockholder is deemed adequately represented. Id. Therefore, this Court believes that as alleged all Merigian's claims are barred by res judicata.

This action is an impermissible collateral attack, especially where the strict limits on direct challenges would bar these claims. 11 U.S.C. 1144 (6 month limitation period). Having failed to raise the claims before, or directly challenge the bankruptcy orders, plaintiffs are without recourse. (2)

Furthermore, even if Merigian's claims were not barred by res judicata, dismissal would be proper. Insofar as the claims in the 1AC arise from fraud or misconduct of the Heller defendants with respect to financing or the bankruptcy proceedings, they are direct injuries to the corporation FSI, indirect injury to SCPI as the shareholder and once-removed indirect injury to Merigian as the shareholder of SCPI. A

---

(2) On the day before oral argument, SCPI plaintiffs filed a motion to amend the 1AC and to stay proceedings pending a decision from the United States Supreme Court in the case In re Ben Cooper. This Court is satisfied that a stay is not appropriate in this case and that the determination whether a jury trial may be held by the bankruptcy court does not affect the decision in this case.

---

shareholder has no standing to bring an action, where the

damage alleged is diminution or destruction of the value of the stock, whether by violation of banking, antitrust, RICO or securities laws, because it is not a direct personal injury. Gaff v. FDIC, 814 F2d 311 (6th Cir. 1987), Warren v. Manufacturers National Bank, 759 F.2d 542 (6th Cir. 1985).

Even the claims which could conceivably be for direct injury, or for which Merigian could conceivably not be in privity with SCPI, any securities fraud claims unrelated to the alleged scheme, would be dismissed for failure to state a claim. The 12(2), 10(b) and Rule 10b-5 claims rest on the factual allegations that Heller certified to the attorneys for SCPI that FSI was a borrower in good standing on which a prospectus issued, but failed to disclose that Heller; had changed its loan standards; would not provide the promised $750,000 in additional loans; used claims of default under the Loan Agreements to extract concessions; would not continue funding; intended to drive FSI into bankruptcy. The Court agrees with defendants that Heller owed no duty to make such disclosures to the purchasers of stock in the shareholder of the debtor, because it was neither a seller of the securities, nor an active participant in the offering. Schlifke v. Seafirst Corp., 866 F.2d 935 (7th Cir. 1989) (citing Pinter v. Dahl, 108 S. Ct. 2063 (1988), Jett v. Sunderman, 840 F2d 1487 (9th Cir. 1988). Thus,

the 12, 10(b) and Rule 10b-5 claims would fail.

Plaintiff Merigian filed a motion for leave to amend the 1AC on the grounds that Merigian had retained separate counsel who would like to "tighten up" the pleading of his claims with more clarify and preciseness. In particular, Merigian mentions the statute of limitations issue and securities fraud claims. Under Fed. R. Civ. P. 15, leave to amend shall be freely given when justice so requires, in order that cases be decided on their merits. Moore v. Paducah, 790 F.2d 557 (6th Cir. 1986). However, leave need not be given if the amendment would be futile or the amended complaint would not withstand a motion to dismiss. Martin v. Associated Truck, 801 F.2d 246 (6th Cir. 1986). At oral argument, counsel for Merigian represented that he did not have claims against Alix, Butzel or Butler, but only against Heller for securities fraud and RICO violations (counts 5, 6, and 7 of the 1AC). He asked for thirty days to file his proposed amended complaint. Merigian's claims have been addressed on the merits and found not to state a cause of action. Merigian's motion for leave to amend the 1AC is DENIED because he has failed to make any offer of allegations, which would survive a motion to dismiss.

Plaintiffs argue that in a second amended complaint

(2AC) they would plead that the plaintiffs were not parties to the bankruptcy proceeding; that the bankruptcy could would not have jurisdiction to hear claims in this action; and that this case is not barred by res judicata. The proposed 2AC filed the day before the argument does make these allegations, however, these are legal conclusions which need not be accepted as true merely because they are pled. Morgan v. Church's Fried Chicken, 829 F.2d 10 (6th Cir. 1989). Accordingly, the late motion to amend the 1AC by the SCPI plaintiffs is DENIED because it cannot survive a motion to dismiss.

ORDER

For the reasons stated in this Court's Memorandum Opinion, the motions to dismiss the complaint by the Heller defendants and Alix are MOOT; the motions to dismiss the first amended complaint by the Heller defendants and Alix are GRANTED; plaintiff Merigian's motion to amend is DENIED; and plaintiffs' motion to amend and for stay of the proceedings is DENIED. Accordingly, the first amended complaint is DISMISSED.

(signed)

_____

George La Plata
U. S. District Judge - Ann Arbor, MI
August 8, 1990

APPENDIX 3

Excerpts from Plaintiffs first amended complaint

satisfying the Metge pleading requirements

COUNT III ABUSIVE EXERCISE OF CONTROL

LIABILITY OF DEFENDANTS HELLER, BUTZEL AND BUTLER

235. Plaintiffs hereby reallege paragraphs 1-234 and Counts IV, V, VI, VII, VIII, XII and XIII, as though fully set forth herein.

236. The Loan Agreement gave considerable control to Heller over the conduct of Sanders, and additional controls were obtained by Heller over Sanders by the subsequent First Amendment, the Interim Operational Letter and the Second Amendment.

237. On July 24, 1986, Defendant Butler informed Sanders on behalf of Defendant Heller that Defendant Heller was declaring Events of Default under the Loan Agreement, was accelerating the maturity date of the Loan, was demanding immediate repayment, and was confirming the suspension of further financing to Sanders.

238. Knowing that Sanders faced economic ruin if

Heller stopped funding, and in a letter dated July 25, 1986, Defendant Butler, on behalf of Defendant Heller, informed Sanders that Heller would dispose of Events of Default under the Loan Agreement and would resume funding to Sanders if Sanders executed the First Amendment to the Loan Agreement.

239. Because Sanders recognized it faced economic ruin if the Heller funding was stopped, because Heller had failed to disclose that its loan standards had changed, Sanders executed the First Amendment to the Loan Agreement on August 29, 1986.

240. Upon information and belief, in a letter written to Sanders on or about December 31, 1986, Defendant Heller claimed that it became aware of a number of defaults, which, if declared, would be Events of Default under the Loan Agreement.

241. Sanders asked Defendant Heller to issue a Waiver and Estoppel Letter in connection with the defaults named in the December 31, 1986 letter.

242. If Defendant Heller did not waive these defaults, Plaintiff SCPI, the parent of Sanders, would have to withdraw and/or materially revise an offering prospectus that was issued in connection with SCPI's public stock

offering to raise additional equity funds to be supplied to Sanders.

243. Knowing that Plaintiff SCPI and Sanders faced economic ruin without its public stock offering, Heller agreed to waive the defaults if Sanders signed an Interim Operational Letter Agreement.

244. Knowing that Plaintiff SCPI and Sanders faced economic ruin without the proceeds of the public stock offering, Sanders executed the Interim Operational Letter Agreement on December 31, 1986.

245. The above conduct on the part of Defendants Heller, Butzel and Butler amounted to abusive exercise of control based, inter alia, upon the following:

(a) Sanders would never have signed the amendments without the threats of termination of funding and immediate acceleration of the loan; (b) Each modification of the loan agreement was more detrimental to Sanders than the preceding arrangement; (c) Heller never advanced the additional funds promised to Sanders even after extracting the amendments to the original loan agreement; and (d) Heller never honored the oral promises made to induce the original loan agreement and its subsequent modifications.

246. There was no substantial showing at any point in

time when these modifications were obtained by Heller that the collateral of Heller was impaired or that other circumstances recognized by the Uniform Commercial Code allowed for termination of funding or acceleration of the loan.

247. The abusive exercise of control by Heller constituted, inter alia,:

(a) Unfair business practices;

(b) Violation of the principles of good faith and fair dealing; and

(c) Violation of fiduciary duties owed to Sanders.

248. Heller, as part of its fiduciary relationship, was under specific duties to Sanders, including, inter alia:

(a) To at all times deal with Sanders in good faith.

(b) To allow Sanders a reasonable opportunity to develop a successful business.

(c) To make known to Sanders its plans with reference to Sanders.

(d) To disclose to Sanders all material facts relating to the

relationship.

249. Heller breached its fiduciary duty to Sanders as plaintiffs in that, inter alia, it:

(a) Refused to correct the lending formula to give Sanders the promised funding; (b) Underfunded Sanders; (c) Extracted from Sanders higher interest than agreed to, penalties, and complete control over Sanders leading to its bankruptcy.

(d) Committed fraud on First Independence Bank, a bridge lender, by making material misrepresentations and by a course of conduct that would defraud First Independence Bank, thereby making sure that the Bank would not have a successful business relationship with Sanders.

(e) Made material misrepresentations with respect to the public offering, in failing to disclose the change in its loan standards, and after receiving all

of the benefits of the public offering that they would receive, put Sanders into bankruptcy. (f) Made material false representations to Sanders that they would cooperate with Sanders in the Chapter 11 bankruptcy proceeding. (g) Forced Sanders to file bankruptcy in order to liquidate Sanders as part of its plan to terminate the loan. (h) Acted in bad faith toward Sanders and plaintiff throughout the bankruptcy proceedings.

250. The wrongful conduct of Heller, Butzel and Butler caused great financial damage to the Plaintiff SCPI by and through the damage caused to its wholly owned subsidiary.

COUNT IV

COMMON LAW FRAUD LIABILITY OF

DEFENDANTS HELLER, UTZEL AND BUTLER

253. At some point in time, shortly after the execution of the initial lending agreement between Sanders and Heller, a decision was made by Heller that the loan to Sanders was a

mistake.

254. Pursuant to said decision, it was decided by Heller to get out of the loan as soon as possible.

255. The problem facing Heller was that the contract with Sanders provided for a loan maturity date of February, 1989, a time far longer than Heller wanted to be a party to the loan.

256. In order to implement the decision to get out of its contract with Sanders, Heller embarked upon a scheme to defraud Sanders by a sophisticated course of conduct.

257. Defendants Butler and Butzel were hired by defendant Heller to guide Heller through its fraudulent scheme by taking precise steps that would tighten Heller's control over Sanders while at the same time enhancing its secured position.

263. Heller's position was enhanced considerably by this First Amendment and by the State of Michigan's subordination agreement in that:

(a) The State of Michigan's subordination to Heller was a major step by defendants in enhancing their position along the road to bankruptcy.

(b) Plaintiff SCPI had to guarantee the loan.

(c) Sanders had to relinquish a cure period to clear up defaults.

(d) All collections from Sanders' operations had to be deposited into Heller's depository account as a "blocked account" where only Heller could make withdrawals.

264. This First Amendment made Heller a "control person" in conducting the affairs of Sanders.

265. Defendants waited to force Sanders into bankruptcy until plaintiff SCPI's public offering was completed, in order that Heller benefit from the offering either directly or indirectly through payment of Sanders' obligations from the proceeds.

267. Defendants continued with their scheme to defraud Sanders without regard to their duties owed to the public in the public stock offering of SCPI by virtue of Heller's position as a "control person" of Sanders and by virtue of their intentional misrepresentations. On December 9, 1986 in a letter sent for the sole purpose of making sure that the public offering went forward, Heller said that Sanders was a borrower in good standing.

268. The letter of December 9, 1986, the letter of December 31, 1986, and the fact that defendants were expecting to benefit from the public offering further gave rise to a duty on the part of defendants to make good faith efforts to help Sanders.

269. The defendants knew that their letters were deliberate misrepresentations

270. Defendants conduct was both a violation of Federal securities laws as set forth herein, and a fraudulent misrepresentation to the shareholders of SCPI.

271. On April 23, 1987, upon Heller's insistence, Sanders agreed to a lock box account for the collection of Sanders' checks and other funds, thereby giving Heller total dominion over Sanders' funds.

272. In August, 1987, after Heller had closed its Detroit

office, Sanders, Filipp Kreissl and John Sanders met with Heller's Chicago representatives. At that meeting, Heller for the first time told Sanders that Heller was no longer interested in loans such as the one with Sanders.

273. On November 5, 1987, Heller sent Sanders a letter stating that Sanders was in default, accelerated the loan and declared the entire amount due in ten days. The letter said that Heller would forbear in the execution of its remedies at the present time. The letter also said that Heller would, on a day-to-day basis in its sole and absolute discretion, provide Sanders with interim stop-gap financing.

274. At this point, Sanders needed working capital funds for the Christmas season without which Sanders would suffer irreparable harm from the loss of the Christmas sales.

278. Heller forced Sanders to file bankruptcy.

279. Heller executed a post-filing loan agreement with Sanders which gave Heller increased control over Sanders' cash flow while Sanders was in bankruptcy.

280. Due to the absolute power over Sanders extracted by defendants as part of their scheme to defraud Sanders, Sanders was unable to thwart Heller's scheme.

281. Despite Trustee Jay Alix's assertions that there was a high probability that Sanders could be successfully reorganized

as a going concern shortly after bankruptcy, Sanders was forced into bankruptcy, Sanders' assets were sold for approximately $3,200,000. This was substantially less than liquidation value.

282. Defendants Heller, Butler and Butzel, through a clever scheme to defraud Sanders and terminate the loan agreement, succeeded in bankrupting Sanders.

THE ACTIONS OF HELLER CAUSED A VIOLATION OF THE SECURITIES ACT OF 1933

LIABILITY OF DEFENDANTS HELLER, BUTZEL AND BUTLER

286. Plaintiffs hereby reallege paragraphs 1-285 and Count XII, as though set forth fully herein.

287. Heller had dominion over the funds of Sanders and control of their operations by virtue of the restrictive loan agreement and its subsequent amendments.

288. As a control person as defined in the 1933 Securities Act, Heller had an absolute duty to insure that there was a full and complete disclosure in the offering prospectus distributed by SCPI of all material facts and also a duty to disclose any change of a material fact.

289. Since defaults had been claimed by Heller, whether valid or invalid, it was necessary for SCPI to obtain a declaration from Heller regarding these defaults in order to

complete the due diligence requirement of the 1933 Act during the preparation of the offering prospectus.

290. Heller certified to the attorneys preparing the SCPI offering prospectus that as of December 9, 1986, Sanders was a borrower in good standing.

291. SCPI delivered a copy of the December 9, 1986 prospectus to the Heller offices for review.

292. In reliance upon the certification of Heller, SCPI issued the security offering prospectus with an effective date of December 9, 1986. On December 31, 1986, Heller notified Sanders that on or about December 18, 1986, it became aware of a number of defaults, which if declared would be Events of Default under the Loan Agreement.

297. The December 31, 1986 waiver from Heller is integrated in the offering prospectus in that the waiver document also provided, "Lender has been informed that borrower will be required to withdraw and/or materially revise a recently issued prospectus issued in connection with a public stock offering if lender is unwilling to waive such defaults."

298. Based on this document, the SCPI stock offering proceeded, and on February 28, 1987, the offering had sold 800,000 shares, which allowed SCPI to break escrow.

299. Prior to the date escrow was broken, Heller

claimed another default in that the note for the over advance of $300,000 for the 1986 Christmas season which matured on January 15, 1987 had not been paid.

300. To avoid the declaration of an Event of Default, Sanders was forced by Heller to execute a Second Amendment to the Loan and Security Agreement for the sole purpose of extending the maturity date of the Christmas loan. This was established as the earliest of (1) February 16, 1987, (2) the maturity date of the underlying term loan agreement, or (3) the date in which the escrow was broken for the public stock offering.

301. Heller having furnished information used in the prospectus was under an affirmative duty to disclose any material change in that information during the life of the offering.

302. Heller did not disclose to Sanders, however, that it had decided that the Sanders loan did not fit Heller's new profile and that Heller intended to extinguish the loan as soon as possible which constituted a material change of circumstance.

303. It was not in Heller's financial interest to disclose the change in its loan standards, because the stock offering proceeds would improve its security position in the meantime.

306. If Heller had declared the above Events of Default, Heller would have had to disclose these material facts to the public. In any event, Heller failed to disclose its change in loan standards affecting the Sanders loan.

307. As consideration for acceptance of the above demands by Sanders, Heller agreed to extend the maturity date of the $300,000 Christmas advance and not declare the Events of Default.

308. Sanders refused to sign its acknowledgment of this February 18, 1987 letter due to the false inferences contained therein but did act on the Heller demands and made concessions to Heller that precluded Heller from declaring the Events of Default.

309. It was not in Heller's financial interest to declare an Event of Default or disclose the material change in circumstances due to the change in loan standards, because the stock offering would benefit Heller.

310. In May, 1987, the offering of SCPI common stock was completed, and this resulted in SCPI raising over $5,000,000 in equity capital

311. The distribution of the proceeds benefited Heller in that additional equity capital was placed under the Heller loan.

312. Heller failed to disclose, inter alia, the following

material facts:

(a) That it had changed its loan standards affecting the Sanders loan.

(b) That Heller was not going to provide the promised $750,000 if $1,000,000 was raised through the offering.

(c) That the claims of defaults were used to extract concessions to the Loan Agreement from Sanders.

(d) That Heller was not going to continue funding Sanders.

(e) That Heller intended to foreclose on the loan as soon as the offering was completed and/or it was feasible.

313. Heller failed to disclose these material facts, because of its own self interest.

314. Due to the position of Heller as a control person, as defined under the 1933 Act, Heller caused Sanders Confectionery Products Inc., as the seller to violate the 1933 Securities Act by causing the issuance of an offering circular

which failed to disclose material facts and subsequent material changes of circumstances.

315. The prospectus made affirmative statements that there were no defaults or that any defaults had been waived creating the impression that the borrower was in good standing and that Heller would continue the financial relationship.

COUNT VI
SECURITIES FRAUD UNDER THE 1934 SECURITIES AND EXCHANGE ACT
LIABILITY OF DEFENDANTS HELLER, BUTZEL AND BUTLER

322. Section 10b and Rule 10b-5 of the Securities Exchange Act of 1934 says "it shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchanges,

(a) to employ any device, scheme or artifice to defraud,

(b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements

made, in the light of thecircumstances under which they were made, not misleading, or

(c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person in connection with the purchase or sale of any security.

323. The defendants herein caused Sanders Confectionery Products Inc, as the Seller, to violate all three of these sections. They employed a scheme to defraud in that they allowed the securities offering to go forward when the Defendants had a "hidden agenda" which operated to the detriment of the purchasers of the securities.

324. As part of their scheme to defraud Sanders, the defendants wrongfully failed to disclose what would have normally been events of default during the "life" of the offering and opted to defer the termination of the Sanders loan until after the public offering of SCPI, the parent of Sanders.

335. Again Heller, as a control person, under a duty by Rule 10b-5 of the 1934 Act to provide information to the public regarding the claims of default that was material to the public offering of SCPI then going on, failed to do so.

336. Because of the scheme to defraud Sanders and the conspiracy entered into by all Defendant, Heller never issued any statement to the public.

337. In addition, Plaintiffs allege that the facts detailed in paragraphs 1 - 336, as realleged herein, clearly indicate that Butler and Heller conspired to defraud the shareholders of Sanders during the "life" of the offering and who purchased the stock in reliance upon the prospectus.

338. Finally, after the offering, Defendants executed their plan which, or engaged in a course of conduct which was designed to terminate the Loan Agreement prematurely and to bankrupt Sanders, and at the same time defraud the shareholders of SCPI.

339. Because of their scheme to defraud Sanders by terminating the Loan Agreement prematurely and by putting it into bankruptcy, Defendants were under a duty to tell the public that any investment in Sanders was going to be greatly diminished, which failure to do so constituted a fraud on the marketplace.

340. Approximately sixty (60) days after the end of the public offering, Heller began the final phase of its scheme to defraud Sanders and the shareholders of SCPI.

341. At the end of August, Heller finally told Sanders

that it was no longer interested in loans such as Sanders'.

342.- Two months later, just before Sanders busy Christmas season, Heller filed a reclamation action in Oakland County Circuit Court for the sole purpose of forcing Sanders into bankruptcy, executing a new, more restrictive loan agreement with Sanders, and continuing the process of acceleration of the maturity date of its loan.

343. Within six months, Sanders' assets were sold off at a fraction of their value, leaving the 3,000 shareholders of SCPI defrauded.

345. The Defendants, because of their relationship with the parties and because they participated in the preparation of the prospectus, had a continuing duty to disclose any material change of circumstance.

346. The defendants deliberately failed to comply either that duty because it was in their best interest not to disclose any information dealing with the changes in circumstances which might negatively effect the public offering.

(2)

Supreme Court, U.S.
FILED
DEC 16 1992
OFFICE OF THE CLERK

No. 92-853

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

SANDERS CONFECTIONERY PRODUCTS, INC., a Michigan corporation; JOHN M. SANDERS; FILIPP KREISSL,
Petitioners,

SAM J. MERIGIAN, on behalf of himself and all persons who were shareholders of Sanders Confectionery Products, Inc., as a Class Action Under FRCP 23(a) and 23(b),
Petitioners,

v.

HELLER FINANCIAL CORPORATION, INC., a Delaware corporation; BUTZEL, KEIDAN, SIMON, MYERS & GRAHAM, a partnership; JOHN WM. BUTLER, JR.; JAY ALIX,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

BRIEF FOR RESPONDENT JAY ALIX IN OPPOSITION

CARSON C. GRUNEWALD
Counsel of Record
BODMAN, LONGLEY & DAHLING
100 Renaissance Center
34th Floor
Detroit, MI 48243
(313) 259-7777
Attorneys for Respondent Jay Alix

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

BEST AVAILABLE COPY

TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	ii
STATEMENT OF THE CASE	1
SUMMARY OF THE ARGUMENT	4
ARGUMENT	4
I. THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT FAILS TO SEEK REVIEW OF ANY CLAIM AGAINST RESPONDENT ALIX AND, CONSEQUENTLY, THIS COURT MUST DENY THE PETITION AS TO JAY ALIX	4
II.	7
CONCLUSION	7
APPENDIX	1a

TABLE OF AUTHORITIES

Cases	Page
Sanders Confectionery Products, Inc., et al. v. Heller Financial, Inc., et al., 973 F.2d 474 (6th Cir. 1992)	3, 6
Statutes	
15 U.S.C. § 77*l*	5-6
15 U.S.C. § 78j	6
28 U.S.C. § 157(b) (1)	6
28 U.S.C. § 157(b) (2) (A)	6
28 U.S.C. § 1334	6
Regulations	
17 C.F.R. 240.10b-5	6
United States Supreme Court Rules	
Rule 14.1(a)	5

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

No. 92-853

SANDERS CONFECTIONERY PRODUCTS, INC., a Michigan corporation; JOHN M. SANDERS; FILIPP KREISSL,
Petitioners,

SAM J. MERIGIAN, on behalf of himself and all persons who were shareholders of Sanders Confectionery Products, Inc., as a Class Action Under FRCP 23(a) and 23(b),
Petitioners,

v.

HELLER FINANCIAL CORPORATION, INC., a Delaware corporation; BUTZEL, KEIDAN, SIMON, MYERS & GRAHAM, a partnership; JOHN WM. BUTLER, JR.; JAY ALIX,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

---

BRIEF FOR RESPONDENT JAY ALIX IN OPPOSITION

STATEMENT OF THE CASE

In December 1987, Jay Alix was appointed Chapter 11 Trustee of Fred Sanders, Inc. ("FSI"). Petitioner Sanders Confectionery Products, Inc. ("SCPI"), was the sole holder of the common stock of FSI. Petitioners Filipp J. Kreissl and John M. Sanders were shareholders of SCPI as well as officers and directors of FSI. Peti-

tioner Sam J. Merigian was a shareholder of SCPI who died in November 1991. Petitioners did not object in the bankruptcy court to Mr. Alix's appointment nor did they seek review of the order appointing him as trustee.

In May 1988, the United States Bankruptcy Court for the Eastern District of Michigan, Southern Division, confirmed a plan of reorganization of FSI under which the assets of FSI were sold to Country Home Bakeries of Michigan, Inc., and SCPI's shareholder interest was extinguished. Petitioners did not appeal from that order of confirmation.

In February 1989, petitioners filed a Complaint in the United States District Court for the Eastern District of Michigan, Southern Division, against respondents, including Mr. Alix, seeking money damages. Petitioners made a variety of claims relating to the plan of confirmation and to matters which occurred prior to the entry of the order confirming the plan of reorganization. Petitioners' claims against Alix all related to his appointment as Trustee or to his administration of FSI's bankruptcy estate prior to entry of the order confirming the plan.

On August 8, 1990, the district court entered a Memorandum Opinion and Order which dismissed all claims against all defendants in that case because such claims arose from the same core of operative facts as FSI's bankruptcy proceedings and because, therefore, such claims were barred by the doctrine of res judicata. Petitioners SCPI, John M. Sanders and Filipp J. Kreissl appealed from that order of dismissal to the United States Court of Appeals for the Sixth Circuit as to all defendants. Petitioner Sam J. Merigian appealed only as to defendant Heller Financial, Inc. Indeed, counsel for Mr. Merigian admitted that Mr. Merigian had made no claim against Mr. Alix. (R. 96, Transcript of 7/27/90 hearing, p. 51).

On August 17, 1992, the court of appeals issued an opinion which affirmed dismissal of all claims and as to

all defendants. *Sanders Confectionery Products, Inc., et al.* v. *Heller Financial Inc., et al.*, 973 F.2d 474 (6th Cir. 1992). In that opinion, the court of appeals specifically held that all of the claims by petitioners SCPI, John M. Sanders and Filipp J. Kreissl against Mr. Alix were to be core proceedings:

> "The claims against the trustee Alix, however, would be core proceedings. . . . All claims against Alix related to his conduct during the FSI bankruptcy, and should be considered core proceedings." *Sanders Confectionery Products*, 973 F.2d 483 n. 4.

Because the Bankruptcy Court would have had jurisdiction to make a final decision on those core proceedings, the court of appeals easily concluded that petitioners' district court claims against Mr. Alix were barred by res judicata. *Id.* at 484-85.

On or about November 16, 1992, petitioners filed a Petition for Writ of Certiorari to the court of appeals. That petition does not, on its face, seek to review the decisions of the courts below regarding petitioners' claims against Mr. Alix. To the contrary, that petition suggests that petitioners do not seek review of claims against Mr. Alix. For instance:

1. Petitioners do not challenge the determination of the court of appeals that all claims against Mr. Alix are core proceedings; and

2. Petitioners' "Questions Presented" and "Reasons for Granting the Writ" relate either to non-core proceedings or to claims by Mr. Merigian (who has admitted having no claim against Mr. Alix and who did not appeal as to Mr. Alix).

Despite those facts, in a letter dated December 8, 1992 (Ex. A), counsel for petitioners indicated his belief that the Petition for Certiorari does include claims against Mr. Alix:

> "All SCPI's claims against all parties, including Alix were precluded by the defendants' assertion of

> res judicata. If the Supreme Court reverses the application of the doctrine of res judicata, all claims including those against Jay Alix were revived."

Although that assertion is totally at odds with the contents of the petition and is patently frivolous, Mr. Alix is compelled by that assertion to submit a response to Petitioners' request for a Petition for Certiorari.

SUMMARY OF THE ARGUMENT

Petitioners do not set forth any issue for this Court's review as to Respondent Jay Alix on their Petition for Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit. Petitioners' Questions Presented address claims which either expressly involve parties other than Respondent Alix or which, by the Questions' contents, address factual and legal questions having no bearing on Mr. Alix.

This Court has stated, through its Rules, that it will consider only issues actually raised in a petitioner's Questions Presented or fairly included therein. As a consequence, Petitioners have failed to ask this Court for relief as to Respondent Alix.

ARGUMENT

I. THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT FAILS TO SEEK REVIEW OF ANY CLAIM AGAINST RESPONDENT ALIX AND, CONSEQUENTLY, THIS COURT MUST DENY THE PETITION AS TO JAY ALIX.

Petitioners do not set forth any reasons in their Petition why this Court should disturb the judgment below in favor of Respondent Jay Alix. In fact, the Petitioners' Questions Presented do not even raise issues relating to Mr. Alix. The Rules of this Court require, therefore that Petitioners' request for a writ of certiorari be denied as to Mr. Alix.

This Court's criteria for review of questions presented in a petition for writ of certiorari are set forth in Rule 14 of the Supreme Court Rules:

> "* * * Only the questions set forth in the petition, or fairly included therein, will be considered by the Court." Rules of the United States Supreme Court, Rule 14.1(a).

The instant Petition neither sets forth a question implicating Mr. Alix nor may such a question be "fairly included" within the text of Petitioners' Questions Presented.

Petitioners present three questions for this Court's review. They are:

> "1. Whether the Court [of Appeals for the Sixth Circuit] erred in holding the Petitioners' non-core issues that are related to the bankruptcy could be adjudicated by the Bankruptcy Court with a jury trial.
>
> "2. Whether a litigant is required to file in Bankruptcy Court and have the Bankruptcy Judge find that the claims are "non-core" and find no subject matter jurisdiction in the face of a jury demand or in the alternative may the litigant file the case directly in District Court, [sic]
>
> "3. Whether the Court [of Appeals for the Sixth Circuit] erred in holding that the Petitioner stockholders [sic] claims were not barred by res judicata or collateral estoppel and hence that the right to a jury trial is not an issue, that the stockholders failed to properly plead that the Respondent Heller was "control person" over the public stock offering thereby dismissing their case for failure to state a claim."

Petition for Writ of Certiorari at i.

Of the three questions presented thus framed, the third clearly has no relevance to Respondent Alix. This question relates solely to Petitioner Merigian's claim under Sections 12(2) of the Securities Act of 1933, 15

U.S.C. § 77*l*, and and 10(b) of the Securities and Exchange Act of 1934, 15 U.S.C. § 78j, and Section 10(b)'s accompanying Rule 10b-5, 17 C.F.R. 240.10b-5. The claims asserted under these statutes and Rule 10b-5 relate to alleged improprieties on the part of Respondent Heller Financial, which in no way implicate Jay Alix. Moreover, Mr. Merigan has conceded that he has no claims against Mr. Alix.

Equally clearly, Petitioners do not raise any issue relating to Mr. Alix in their first two Questions Presented. These questions address themselves only to the issue of the proper situs for the adjudication of "non-core" proceedings arising under the Bankruptcy Code. *See* 28 U.S.C. § 157(b)(1). Petitioners argue throughout their petition that, as to non-core proceedings, the district court deprived them of their right to a jury trial simply because of what petitioners perceive to be confusion on the part of the lower courts as to the effect of the interplay between the provisions creating the "core"/"non-core" distinction, 28 U.S.C. § 157(b)(1), and the statute establishing the original, if not exclusive, jurisdiction of the district courts in bankruptcy proceedings, 28 U.S.C. § 1334(b).

Regardless, however, of the disposition of this question, there can be no question that claims relating to Respondent Alix's duties as trustee of the bankruptcy estate of FSI are themselves core proceedings under 28 U.S.C. § 157(b)(2)(A) (stating that claims relating to the administration of the bankruptcy estate are core proceedings). Both the district court and the court of appeals, below, correctly reached this conclusion. *See, e.g., Sanders Confectionery Products*, 973 F.2d 474, 483 n.4. As core proceedings therefore, Mr. Alix's actions are not addressed in Petitioners' Questions Presented Nos. 1 & 2, which are limited in scope to non-core proceedings.

II.

As for the remaining issues addressed by Petitioners, Respondent Alix concurs in the response of Respondents Heller Financal, Inc., to be filed.

CONCLUSION

Petitioners fail to raise issues for this Court's consideration with respect to Respondent Jay Alix. Respondent Alix respectfully prays, therefore, that this Honorable Court affirm the judgment of the United States District Court for the Eastern District of Michigan with respect to Respondent Alix and dismiss the Petition for Writ of Certiorari.

CARSON C. GRUNEWALD
Counsel of Record
BODMAN, LONGLEY & DAHLING
100 Renaissance Center
34th Floor
Detroit, MI 48243
(313) 259-7777
Attorneys for Respondent
Jay Alix

APPENDIX

Richard L. Roble JD, PC
A Professional Corporation
Attorney At Law
Admitted Georgia and Michigan

The Taggart Building—1719 Abercorn St. Savannah, GA 31412
Mailing Address—P.O. Box 10033 Savannah, GA 31412-0233
Direct Phone (912) 232-7722 Fax (912) 232-1441

8 December, 1992

David Chardavoyne
Bodman, Longley & Dahling

via fax (313) 393-7579

RE: In Re Fred Sanders Inc
Sanders v Heller & Alix

Dear David:

It was nice seeing you again. Hopefully we made some steps favorable to both of us.

I was unable to address your questions regarding the cert issues because I was focused on the bankruptcy proceedings.

All SCPI's claims against all parties including Alix were precluded by the defendants' assertion of res judicata. If the Supreme Court reverses the application of the doctrine of res judicata, all claims including those against Jay Alix are revived.

Warmest regards,

Richard L. Roble

(no signature because sent directly from computer)

(3)

Supreme Court, U.S.
FILED
DEC 23 1992
OFFICE OF THE CLERK

No. 92-853

In the Supreme Court of the United States

October Term, 1992

SANDERS CONFECTIONERY PRODUCTS INC., a Michigan corporation; JOHN M. SANDERS; FILIPP KREISSL,
Petitioners,

SAM J. MERIGIAN, on behalf of himself and all persons who were shareholders of Sanders Confectionery Products, Inc., as a Class Action Under FRCP 23(a) and 23(b),
Petitioner,

v.

HELLER FINANCIAL, INC., a Delaware corporation; BUTZEL, KEIDEN, SIMON, MYERS & GRAHAM, a Michigan partnership; JOHN WM. BUTLER JR.; JAY ALIX,
Respondents.

On Petition for Writ of Certiorari to
The United States Court of Appeals for the Sixth Circuit

BRIEF OF RESPONDENTS, HELLER FINANCIAL, INC., BUTZEL, KEIDEN, SIMON, MYERS & GRAHAM, and JOHN WM. BUTLER, JR., IN OPPOSITION

NORMAN H. NACHMAN*
DAN K. WEBB
GERALD F. MUNITZ
TIMOTHY J. RIVELLI
PETER C. McCABE III
WINSTON & STRAWN
35 West Wacker Drive
Chicago, IL 60601
(312) 558-5600
Attorneys for Respondents
Heller Financial, Inc., Butzel, Keidan, Simon, Myers & Graham, and John Wm. Butler, Jr.

*Counsel of Record

31pp

COUNTERSTATEMENT OF THE QUESTIONS PRESENTED

In May, 1988, the United States Bankruptcy Court for the Eastern District of Michigan entered an Order confirming a reorganization plan for a chapter 11 debtor, Fred Sanders, Inc. ("FSI"). Nine months later, Sanders Confectionery Products, Inc. ("SCPI"), the parent of FSI, as well as two of SCPI's directors and officers, and one of its stockholders, all Petitioners herein, brought an action in the United States District Court for the Eastern District of Michigan against FSI's lender, Heller Financial, Inc. ("Heller"), Heller's attorneys, John Wm. Butler, Jr. ("Butler") and his firm, Butzel, Keiden, Simon, Myers & Graham ("Butzel, Keiden"), and FSI's bankruptcy trustee, Jay Alix, alleging claims of "lender liability", federal securities fraud, and RICO. The district court dismissed the action, holding that it was barred by the doctrine of *res judicata*. The district court also dismissed the federal securities fraud and RICO claims on the alternate ground that the factual allegations purportedly supporting these charges did not state any claim upon which relief could be granted. The United States Court of Appeals for the Sixth Circuit affirmed the district court's dismissal of Petitioners' claims.

In this challenge to the *res judicata* effect of the Confirmation Order entered in the FSI chapter 11 case, the questions presented are as follows:

1. Whether the district court and the court of appeals properly determined that Petitioners' claims of lender liability, federal securities fraud, and RICO should have been brought in the FSI chapter 11 case and, therefore, were barred by the doctrine of *res judicata* when asserted in the subsequent district court action?

2. Whether the district court and the court of appeals properly rejected Petitioners' arguments that the doctrine of *res judicata* could not bar their claims because certain of those claims would have been "related proceedings" and not "core proceedings" if the claims had been asserted in the FSI chapter 11 case?

3. Whether the court of appeals properly affirmed the dismissal of Petitioner Merigian's federal securities fraud claims because he failed to plead sufficient facts in the district court which would establish that Heller was liable to Merigian as a "controlling person" of SCPI, the primary perpetrator of Petitioners' alleged stock fraud?

RULE 29.1 STATEMENT

Petitioner Sanders Confectionery Products, Inc. is a publicly-held corporation with its principal place of business in Detroit, Michigan. Respondents are unaware of any parent, subsidiary, or affiliate corporations of SCPI.

Respondent Heller Financial, Inc. is a wholly-owned subsidiary of Heller International, Inc., which is a wholly-owned subsidiary of The Fuji Bank, Limited.

TABLE OF CONTENTS

Page

COUNTERSTATEMENT OF THE QUESTIONS PRESENTED 1

RULE 29 1 STATEMENT iii

TABLE OF CONTENTS iv

TABLE OF AUTHORITIES vi

COUNTERSTATEMENT OF JURISDICTION 2

CONSTITUTIONAL, STATUTORY AND PROCEDURAL RULES INVOLVED 2

COUNTERSTATEMENT OF THE CASE 4
- Nature of the Case 4
- Facts Giving Rise to This Lawsuit 5
- Course of This Litigation Below 9

SUMMARY OF ARGUMENT 12

REASONS WHY THE PETITION SHOULD BE DENIED 14

I NEITHER THE DECISIONS BELOW NOR THE RECORD RAISES THE FIRST QUESTION PRESENTED IN THE PETITION 14

Page

II THE COURT OF APPEALS CORRECTLY APPLIED THE DOCTRINE OF RES JUDICATA TO THE CLAIMS OF PETITIONERS SCPI, SANDERS, AND KREISSL AND ITS DECISION THAT THE FSI CONFIRMATION ORDER BARS CLAIMS WHICH WOULD HAVE BEEN "NON-CORE" IF ASSERTED THEREIN IS IN ACCORD WITH THE JURISDICTIONAL GRANT TO THE DISTRICT COURTS OVER ALL MATTERS RELATED TO BANKRUPTCY CASES 15

III THE COURT OF APPEALS CORRECTLY DECIDED THAT, DESPITE HIS EXTENSIVE ALLEGATIONS IN THE DISTRICT COURT, PETITIONER MERIGIAN FAILED TO STATE A CLAIM OF CONTROLLING PERSON LIABILITY AGAINST HELLER UNDER THE FEDERAL SECURITIES LAWS 18

CONCLUSION 20

APPENDIX A

TABLE OF AUTHORITIES

Cases

Barnett v. Stern, 909 F.2d 973 (7th Cir. 1990) 17

Chicot County Drainage Dist. v. Baxter State Bank, 308 U.S. 371 (1940) 16

Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976) 5, 11

Eubanks v. F.D.I.C., 977 F.2d 166 (5th Cir. 1992) 17

Federated Dept. Stores v. Moitie, 452 U.S. 394 (1981) 16

In the Matter of Kroner, 953 F.2d 317 (7th Cir. 1992) 17

In the Matter of Muller, 851 F.2d 916 (7th Cir. 1988), *cert. denied*, 490 U.S. 1007 (1989) 14-15

Irvin v. Airco Carbide, 837 F.2d 724 (6th Cir. 1987) 15

King v. South Central Bell Tel. & Tel. Co., 790 F.2d 524 (6th Cir. 1986) 16

K-Mart Corp. v. Oriental Plaza, Inc., 875 F.2d 907 (1st Cir. 1989) 15

Metge v. Baehler, 762 F.2d 621 (8th Cir. 1985), *cert. denied*, 474 U.S. 1057 (1986) 18, 19

Oneida Motor Freight, Inc. v. United Jersey Bank, 848 F.2d 414 (3d Cir.), *cert. denied*, 488 U.S. 967 (1988) 16

Sanders Confectionery Products, Inc. v. Heller Financial, Inc., 973 F.2d 474 (6th Cir. 1992) 10-11, 16

Schlifke v. SeaFirst Corp., 866 F.2d 935 (7th Cir. 1989). 19

Cases

Stoll v. Gottlieb, 305 U.S. 165 (1938) 10, 16

Sure-Snap Corp. v. State Street Bank & Trust Co., 948 F.2d 869 (2d Cir. 1991) 17

Statutes

11 U.S.C. §1126 8

11 U.S.C. §1129 8

15 U.S.C. §77l(2) 9, 13, 18

15 U.S.C. §78j 5, 9, 13, 18

18 U.S.C. §§151-55 9

18 U.S.C. §1961 *et seq* 5, 9

28 U.S.C. §151 17

28 U.S.C. §157 . . . . . 3-4, 10, 13, 14, 17

28 U.S.C. §1254 2

28 U.S.C. §1291 10

28 U.S.C. §1331 12

28 U.S.C. §1334(a) 2-3, 12

28 U.S.C. §1334(b) 3, 10, 12-13, 14, 17

28 U.S.C. §2101(c) 2

Regulations

17 C.F.R. 240.10b-5 5

Federal Rules of Civil Procedure

Rule 12(b)(6) . . . . . passim

Rule 38(d) 4, 14

Rule 54(a) 8

Rules **Page(s)**

United States Supreme Court Rules

Rule 24.2 4

Rule 35.1 2

Bankruptcy Rules

Rule 7054 8

No. 92-853

In the

Supreme Court of the United States

October Term, 1992

SANDERS CONFECTIONERY PRODUCTS, INC., et al.,
Petitioners,

v.

HELLER FINANCIAL, INC., et al.,
Respondents.

On Petition for Writ of Certiorari
To The United States Court of Appeals for the Sixth Circuit

BRIEF OF RESPONDENTS IN OPPOSITION

Respondents, Heller Financial, Inc., Butzel, Keiden, Simon, Myers & Graham, and John Wm. Butler, Jr. (collectively, Heller), respectfully request that this Court deny the Petition for Writ of Certiorari which seeks review of the August 17, 1992 Opinion of the United States Court of Appeals for the Sixth Circuit in this cause.

OPINIONS BELOW

The Sixth Circuit's Opinion is reported at 973 F.2d 474 (6th Cir. 1992). The Memorandum Opinion and Order of the United States District Court for the Eastern District of Michigan is not reported.

COUNTERSTATEMENT OF JURISDICTION

Heller agrees with Petitioners that this Court has jurisdiction to review the petition for writ of certiorari filed by Petitioners Sanders Confectionery Products, Inc., John M. Sanders, and Filipp Kreissl (collectively "SCPI") pursuant to 28 U.S.C. §§1254(1) and 2101(c).[1]

In this case, Petitioners invoked the original jurisdiction of the district courts to hear cases involving federal questions pursuant to 28 U.S.C. §1331. Contrary to Petitioners' repeated suggestions in their Petition, this case does not in any way arise from the denial of a demand for a jury trial made during the course of a bankruptcy case.

CONSTITUTIONAL, STATUTORY AND PROCEDURAL RULES INVOLVED

Title 28 of the United States Code, Sections 1334(a), (b) provide:

> §1334. Bankruptcy cases and proceedings
>
> (a) Except as provided in subsection (b) of this section, the district courts shall have original

---

1 Respondents respectfully suggest that the Court is without jurisdiction to review the Petition purportedly filed by Petitioner Sam Merigian because Respondents believe that Merigian died on November 18, 1991, more than six months ago, and no proper substitution has been made on his behalf in this Court pursuant to Rule 35.1. Heller respectfully suggests, therefore, that Merigian's Petition is either moot or his claims have abated. A copy of Merigian's Death Certificate is attached as Respondents' Appendix A. Further the fact that Merigian filed his case as a class action on behalf of himself and all other SCPI stockholders similarly situated does not affect the mootness of Merigian's Petition because the District Court never certified this case as a class action.

and exclusive jurisdiction of all cases under title 11.

(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

Title 28 of the United States Code, Sections 157(a), (b)(1), (c)(1), and (d) provide, in relevant part:

§157. Procedures

(a) Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.

(b) (1) Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.

* * * * *

(c) (1) A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de

> novo those matters to which any party has timely and specifically objected.
>
> * * * * *
>
> (d) The district court may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown. The district court shall, on timely motion of a party, so withdraw a proceeding if the court determines that resolution of the proceeding requires consideration of both title 11 and other laws of the United States regulating organizations or activities affecting interstate commerce.

The Seventh Amendment to the United States Constitution provides, in relevant part:

> In Suits at common law, where the value in controversy shall exceed twenty dollars, the right to trial by jury shall be preserved . . . .

Rule 38(d) of the Federal Rules of Civil Procedure provides, in relevant part:

> (d) Waiver. The failure of a party to serve a demand as required by this rule and to file it as required by Rule 5(d) constitutes a waiver by the party of trial by jury . . . .

COUNTERSTATEMENT OF THE CASE[2]

Nature of the Case

In this case, the United States Court of Appeals for the Sixth Circuit held that the district court properly concluded that

---

2 Pursuant to Supreme Court Rule 24.2, Respondents submit this Counterstatement of the Case to correct inaccuracies and omissions in the Statement of the Case set forth in the Petition for Writ of Certiorari.

the doctrine of *res judicata* barred all claims asserted by Petitioners SCPI, Sanders, and Kreissl, based on a final judgment entered by the United States Bankruptcy Court for the Eastern District of Michigan confirming a plan of reorganization involving the chapter 11 debtor, FSI. In reaching this conclusion, the court of appeals applied the proper legal test utilized by the federal courts in determining whether a claim is barred by *res judicata*. Petitioners do not contest in their Petition that the *res judicata* analysis engaged in by the court of appeals was contrary to established law.

The Sixth Circuit also held that the district court properly dismissed Petitioner Merigian's federal securities fraud and RICO claims because, under existing law (a) Merigian failed to plead sufficient facts in the district court to establish a "control relationship" between Heller and SCPI, the alleged primary violator of the federal securities laws (as well as a Petitioner in this Court), (b) Merigian failed to plead any facts demonstrating that SCPI acted with the requisite scienter in connection with its alleged violation of Section 10(b) of the 1934 Securities Exchange Act, §15 U.S.C. §78j, and Rule 10b-5 promulgated thereunder, 17 C.F.R. 240.10b-5, as required by the Court's decision in *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976), and (c) Merigian failed to allege sufficient facts in the district court to establish that Heller committed any predicate acts which would constitute a violation of the federal RICO statute, 18 U.S.C. §1961 *et seq.* By their Petition for a writ of certiorari, Petitioners have asked this Court to review the court of appeals' decision that the district court correctly applied the law to their claims.

Facts Giving Rise to This Lawsuit

On February 15, 1986, Heller and FSI entered into a Loan and Security Agreement (hereinafter "Loan Agreement") pursuant to which Heller provided a loan to FSI in an amount up to $2.45 million. SCPI was the parent and sole shareholder of FSI. Petitioner Sanders is chairman of the board of SCPI and held the same position at FSI at all times relevant to this case. Petitioner Kreissl is president of SCPI and held the same position at FSI.

Respondent Butzel, Keiden and one of its partners, Respondent John Wm. Butler, Jr., were Heller's attorneys and represented Heller throughout most of its discussions and negotiations with FSI regarding the Loan Agreement.

In late 1986 and early 1987, SCPI, the parent of FSI, engaged in a public stock offering which, according to Petitioners, was quite successful. SCPI issued a prospectus in connection with its stock offering with an effective date of December 9, 1986. Petitioners alleged in the district court that "Heller certified as of December 9, 1986 that [FSI] was a borrower in good standing." This "certification" apparently was made in a letter sent to the attorneys preparing the SCPI offering prospectus. Petitioners did not plead any other facts in the district court relating to Heller's involvement in the preparation of the SCPI prospectus. Heller was not alleged to have sold any securities to Petitioners or to have participated in the sale of SCPI stock to any person. In fact, Petitioners Sanders and Kreissl did not allege in the district court that they ever purchased any SCPI stock during the offering even though they also brought federal securities fraud claims against Heller in the district court. Despite the success of SCPI's public offering, by November 1987, FSI had defaulted on its obligations under the parties' Loan Agreement and, on November 13, 1987, Heller filed a claim and delivery action against FSI in the Circuit Court of Oakland County, Michigan to foreclose on its loan to FSI. On November 16, 1987, six months *after* the completion of the SCPI stock offering, FSI filed a petition seeking relief under chapter 11 of the Bankruptcy Code in the U.S. Bankruptcy Court for the Eastern District of Michigan.[3]

After proper notice, the Bankruptcy Judge held a hearing on November 20, 1987 on FSI's Motion for Authorization for Debtor-In-Possession to Borrow Funds. At this hearing, FSI was represented by counsel. The bankruptcy court subsequently entered a "Consent Order Authorizing Debtor-in-Possession to Bor-

---

3 The bankruptcy case was entitled *In the Matter of Fred Sanders, Inc.*, Case No. 87-06979-B, the Honorable George Brody, presiding.

row Funds From First Secured Creditor, etc." (hereinafter "Consent Financing Order").

The Consent Financing Order approved and incorporated by reference the Post-Petition Loan and Security Agreement previously executed by Heller, FSI and Petitioners SCPI, Sanders, and Kreissl (hereinafter "Post-Petition Loan Agreement"). The Post-Petition Loan Agreement permitted Heller to provide discretionary interim financing to FSI during the pendency of the chapter 11 case. In exchange for post-petition financing, FSI, SCPI, Sanders and Kreissl agreed that they had "no claims, setoffs or defenses" to Heller's exercise of any of its rights as a creditor. FSI, SCPI, Sanders, and Kreissl also agreed to waive any claims or defenses relating to FSI's obligations to Heller and any claims which contested "the conduct of [Heller] in administering the Financing Arrangements or otherwise."

On December 4, 1987, the Creditors' Committee and Heller, believing that cause existed to replace existing management, moved to appoint an operating trustee for FSI. At the hearing on this motion, FSI, again represented by counsel, made no objection. The bankruptcy court appointed Jay Alix as Trustee. Within one week after his appointment as Trustee of FSI, Alix discharged Kreissl and assumed control of FSI's business.

The bankruptcy court subsequently held an extensive hearing on the objections to the Consent Financing Order on December 21, 1987. Following further negotiations among the parties in interest, and two additional hearings before the court, on January 7, 1988, the bankruptcy court entered a "Supplemental Consent Order Amending and Confirming Initial Financing and Adequate Protection Order" (hereinafter "Supplemental Consent Financing Order"). The Supplemental Consent Financing Order was approved as to form and substance by FSI's counsel, as well as by the Trustee, Heller and a number of other creditors. In this order, the bankruptcy court "confirmed, approved and ratified" the earlier Consent Financing Order, and determined that Heller's claims under the Loan Agreement were valid and "not subject to any claims, set-offs or defenses by [FSI]." Additionally, the Order "forever barred" all parties in interest from suing Heller for any

claims "arising or related to its Loan Agreement with FSI." The bankruptcy court also specifically determined that the Supplemental Consent Financing Order was a final order "in accordance with Bankruptcy Rule 7054 and Federal Rule of Civil Procedure 54(a)." No appeal was taken from the entry of the Supplemental Consent Financing Order nor was its reconsideration ever sought.

On April 27, 1988, the bankruptcy court held a hearing on the three competing plans of reorganization for FSI, one of which was proposed by Petitioners SCPI, Sanders, and Kreissl. At this hearing, SCPI withdrew its plan because it had failed to deposit $500,000 in earnest money as required by a prior order of the bankruptcy court. The bankruptcy court was then advised that the reorganization plan proposed by Trustee Alix had been withdrawn in favor of a plan proposed jointly by the union representing FSI's workers and Country Home Bakery of Michigan, Inc. Following a full hearing, and in strict compliance with 11 U.S.C. §1129, the bankruptcy court confirmed the Union/Country Home Plan and entered an "Order Confirming Third Amended Plan of Reorganization of the United Distributive Workers, Council 30" on May 4, 1988 (hereinafter "Confirmation Order"). The Confirmation Order contains an express finding that the Union/Country Home Plan had been "proposed in good faith" and "not by any means forbidden by law."

The Confirmation Order approved the classification and treatment of different classes of claims and interest. All holders of FSI capital stock, *i.e.*, SCPI, were placed in "Class 10" and their interests were "extinguished." The holders of Class 10 claims objected to the treatment of their claims and by reason of the extinguishment of their interests, were deemed to have rejected the Union/Country Home Plan under 11 U.S.C. §1126(g). The Confirmation Order was properly entered over the shareholder's objection pursuant to the power contained in Section 1129(b)(2)(C) of the Bankruptcy Code. The assets of the Debtor's estate and the name "Fred Sanders" were then sold on May 20, 1988 to Country Home pursuant to the Confirmation Order and Country Home continues to operate the business today. Although they were deemed to be parties to the FSI chapter 11 case, Peti-

tioners SCPI, Sanders, and Kreissl never asserted or scheduled any lender liability, securities fraud, or RICO claims during the FSI chapter 11 case. Also, Petitioners never timely demanded a jury trial on any claim they could have asserted in the FSI chapter 11 case.

Course of This Litigation Below

Petitioners sued Heller, Butzel, Keiden, and Butler in the United States District Court for the Eastern District of Michigan in February 1989, approximately eight months after the entry of the Confirmation Order and more than two years after the SCPI stock offering. Jay Alix, the Trustee for FSI in its chapter 11 case, was also sued by Petitioners for his alleged complicity in the bankruptcy court's entry of the Confirmation Order approving the sale of FSI's assets to Country Home. In their various complaints filed in the district court, Petitioners sought relief under a variety of state and federal statutes, including claims brought under the 1933 Securities Act, 15 U.S.C. §77l(2), the 1934 Securities Exchange Act, 15 U.S.C. §78j, the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. §1961 *et seq.*, the federal criminal statutes prohibiting bankruptcy fraud, 18 U.S.C. §§151-155, and various pendent state law "lender liability" claims. On August 8, 1990, the district court dismissed all of Petitioners claims pursuant to Respondents' Rule 12(b)(6) motions to dismiss. In its Memorandum Opinion and Order granting Respondents' motion to dismiss (hereinafter "Mem. Op. & Order", Petitioners' Appendix-2), the district court concluded that SCPI's claims were clearly barred by *res judicata* as a result of final orders entered in the FSI chapter 11 case. Mem. Op. & Order at p. 16. The district court also held that Merigian's claims were barred by *res judicata* because he was in privity with SCPI. *Id.* at p. 16-17. As an alternate ground for dismissing Merigian's claims, the district court concluded that Merigian had no standing to raise any of his claims because they were derivative to those of SCPI or FSI. *Id.* at 17-18. Further, the district court concluded that, even if Merigian's federal securities fraud claims were not barred by *res judicata*, or were not derivative to those of SCPI, those causes of action, as pled in his complaint, did not state any

claim upon which relief could be granted. *Id.* at 18-19. The district court also denied Merigian's pending motion for leave to file an amended complaint because he "failed to make any offer of allegations, which would survive a motion to dismiss." *Id.* at p. 19. All plaintiffs timely filed their notices of appeal from the district court's decision in the United States Court of Appeals for the Sixth Circuit, which properly exercised jurisdiction over the case pursuant to 28 U.S.C. §1291.

The court of appeals affirmed the district court's decision granting Respondents' Rule 12(b)(6) motions to dismiss. *Sanders Confectionery Products, Inc. v. Heller Financial, Inc.*, 973 F.2d 474 (6th Cir. 1992). The court of appeals held that the district court correctly determined that the doctrine of *res judicata* barred the claims of Petitioners SCPI, Sanders, and Kreissl. 973 F.2d at 484-85. The court of appeals ruled that, under this Court's decision in *Stoll v. Gottlieb*, 305 U.S. 165 (1938), an order confirming a reorganization plan in a bankruptcy case is a final judgment for *res judicata* purposes. *Id.* at 480. The court of appeals also ruled that, under existing case law in the circuit courts of appeal, Petitioners SCPI, Sanders, and Kreissl were parties to the FSI chapter 11 case. *Id.* at 481. The court of appeals further determined that the claims asserted by SCPI in the district court were identical to the claims which were either raised or could have been raised in the FSI chapter 11 case. *Id.* at 483-84. In reaching this conclusion, the court of appeals rejected Petitioners' contention that their "lender liability", federal securities fraud, and RICO claims were not identical to the matters at issue in the FSI chapter 11 case and could not have been asserted in the bankruptcy court because they would have been "non-core" proceedings. *Id.* at 482-83. The court of appeals held that, even though a bankruptcy court may not have subject matter jurisdiction over "non-core" proceedings, because the claims at issue were clearly related to the FSI chapter 11 case, they fell within the bankruptcy jurisdiction of the district courts under 28 U.S.C. §1334(b) and could have been determined by the district court pursuant to 28 U.S.C. §157(c) or (d), if Petitioners had asserted such claims. *Id.* at 483. Thus, the court of appeals concluded that the Confirmation Order entered in the FSI chapter 11 case barred all SCPI's

claims, both "core" and "non-core", because the claims were related to the FSI chapter 11 case and, therefore, fell within the district court's general bankruptcy jurisdiction. *Id.* Contrary to Petitioner's suggestion, the court of appeals never addressed the question of whether the bankruptcy court could have conducted a jury trial over their "non-core" claims because Petitioners did not bring their claims in the FSI chapter 11 case and, of course, never demanded a jury trial on these alleged claims.

The court of appeals also ruled that the district court improperly dismissed Petitioner Merigian's claims on the grounds of *res judicata* because the issue of whether Merigian was in privity with SCPI or whether his interests were adequately represented by SCPI in the FSI chapter 11 case was a question of fact which should not have been resolved on a Rule 12(b)(6) motion to dismiss. *Id.* at 482. Nevertheless, the court of appeals held that the district court properly dismissed Merigian's federal securities fraud and RICO claims against Heller because he failed to plead any facts which would entitle him to relief under these statutes. Specifically, the court of appeals determined that, given the numerous and explicit factual allegations made by Merigian in the district court, dismissal of Merigian's claims under Section 12(2) of the 1933 Securities Act and Section 10(b) of the 1934 Securities Exchange Act, which were premised on a "controlling-person" liability theory, was proper because, under existing case law in the circuit courts of appeal, Heller's conduct in administering its loan to FSI could not, as a matter of law, constitute "control" over SCPI necessary for liability to attach under the federal securities laws. *Id.* at 485-86. Further, the court of appeals held that Heller could not be liable for an alleged Rule 10b-5 violation on an "aiding and abetting" theory because Merigian failed to allege that SCPI, the primary securities fraud violator, acted with scienter or "an intent to deceive, manipulate or defraud" as required by the Court's decision in *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976). *Id.* at 486. Finally, the court of appeals ruled that Merigian's RICO claims were properly dismissed because he failed to allege properly any predicate acts which would constitute a RICO violation. *Id.* at 487. The court of appeals' August 17, 1992 Opinion and Judgment was thus is-

sued as the court's Mandate on September 9, 1992. The instant Petition for writ of certiorari followed.

SUMMARY OF ARGUMENT

Petitioners suggest that their Petition for a writ of certiorari should be granted to resolve the question of whether bankruptcy judges, who are not Article III judges, may conduct jury trials. While this issue is important to bankruptcy administration, it is totally irrelevant to the determination of this case.

The district court's jurisdiction in this case was invoked by Petitioners pursuant to 28 U.S.C. §1331 (which grants original jurisdiction to the district courts in cases involving federal questions), and not under 28 U.S.C. §1334 (which grants jurisdiction to the district courts over all bankruptcy cases and proceedings). This non-bankruptcy case, which was dismissed prior to trial, is simply not the vehicle for deciding whether a bankruptcy judge may constitutionally preside over a jury trial.

Petitioners' second argument as to why the Court should grant their Petition is that the courts below erred in applying the doctrine of *res judicata* to this case, which they claim resulted in the improper dismissal of their claims. There are four elements to the doctrine of *res judicata*: (1) a final judgment on the merits; (2) identical parties or privies; (3) the second action raises a claim which was actually litigated or should have been litigated in the first action; and (4) identity of the causes of action. Petitioners' specific contention of error in their Petition is that the third element, requiring that the subsequent action involve a claim which should have been litigated in the first action, is lacking. Petitioners' argue that the claims asserted in this case could not have been brought during the FSI chapter 11 case because the bankruptcy court would have not been able to exercise subject matter jurisdiction over their claims, if these claims had been asserted.

Petitioners' argument fails to recognize the distinction carefully drawn by the court of appeals in this case between the jurisdictional grant over all civil proceedings "arising in or related to cases under title 11" vested in the district courts by 28 U.S.C.

§1334(b) and the allocation of that jurisdiction between the Article III district judges and the Article I bankruptcy judges, which is set forth in 28 U.S.C. §157.

The bankruptcy court's jurisdiction to administer the FSI chapter 11 case and its authority to have entered the Confirmation Order is indisputable. The purported claims asserted by Petitioners in this case either arose prior to or during the course of the FSI chapter 11 case, and these claims could have, and should have, been asserted therein either as an independent proceeding or as an objection to the confirmation of the plan of reorganization. That Petitioners' claims or objections might not have been "core proceedings" and, therefore, would have been treated as related proceedings under 28 U.S.C. §157(c), or heard in their entirety by a district judge because of the mandatory withdrawal requirements of 28 U.S.C. §157(d), does not alter the uncontested fact that the district court had the jurisdiction to hear and determine any civil proceeding arising in or related to the FSI chapter 11 case. The existence of the third element of *res judicata* is to be determined by the jurisdiction of the first tribunal to hear a claim, and not which judicial officer of that tribunal renders the decision. Petitioners could have asserted their claims against Heller in the FSI chapter 11 case, and thereby, under *res judicata*, are prohibited from doing so in this case.

If the Court decides that it has jurisdiction to consider Petitioner Merigian's federal securities fraud claims, his Petition for a writ of certiorari should be denied because the only issue raised in his petition does not warrant review by the Court. Petitioner Merigian does not claim that the court of appeals' decision that the district court properly dismissed his "controlling person" claims under Section 12(2) of the 1933 Securities Act and Section 10(b) of the 1934 Securities Exchange Act is in conflict with any decision of this Court or in conflict with the decision of any other circuit court of appeals. The court of appeals correctly affirmed the dismissal of Merigian's "controlling person" claims because Heller could not, as a matter of law, control SCPI based solely on Heller's administration of its Loan Agreement with FSI, which is what Merigian alleged in the district court.

REASONS WHY THE PETITION SHOULD BE DENIED

I. NEITHER THE DECISIONS BELOW NOR THE RECORD RAISES THE FIRST QUESTION PRESENTED IN THE PETITION.

The first question presented in the Petition is

> "Whether the Court erred in holding the Petitioners' non-core issues that are related to the bankruptcy could be adjudicated by the Bankruptcy Court with a jury trial."

However, the Sixth Circuit did not decide that question in this case. Moreover, the facts in the record will not support a determination of that question by this Court.

In its Opinion, the Sixth Circuit held that the Confirmation Order entered by the bankruptcy court in the FSI chapter 11 case was a final judgment which barred all claims which Petitioners SCPI, Sanders, and Kreissl either brought or could have asserted in the bankruptcy case, regardless of whether the claims are deemed "core" or "non-core" under 28 U.S.C. §157. The Sixth Circuit correctly concluded that because SCPI's claims asserted in this action were clearly related to the FSI chapter 11 case, the bankruptcy court and district court, if necessary, could properly have exercised subject matter jurisdiction over Petitioners' claims under 28 U.S.C. §1334(b). Therefore, because SCPI, Sanders, and Kreissl were parties to the FSI chapter 11 case, their claims asserted in this action are barred by *res judicata*.

It is undisputed that SCPI, Kreissl, and Sanders did not assert their purported lender liability, or any other, claims against Heller in the FSI chapter 11 case. It is also undisputed that Petitioners did not timely demand a jury on any claim they could have asserted in the FSI chapter 11 case under Rule 38 of the Federal Rules of Civil Procedure. Under Rule 38(d), Petitioners' failure to demand timely a jury constitutes a waiver of their right to a jury trial. *See In the Matter of Muller*, 851 F.2d 916, 919-20

(7th Cir. 1988), *cert. denied*, 490 U.S. 1007 (1989); *see also K-Mart Corp. v. Oriental Plaza, Inc.*, 875 F.2d 907, 914 (1st Cir. 1989); *Irvin v. Airco Carbide*, 837 F.2d 724, 727 (6th Cir. 1987). Thus, Petitioners have failed to preserve for review any right to a jury trial they might have had regarding any "non-core" claim they should have asserted in the FSI chapter 11 case.

It is further undisputed that Petitioners were not denied any jury trial rights in this action since their claims were dismissed prior to trial. Thus, Petitioners' suggestion to the Court that this case presents an opportunity for the Court to decide the difficult issue of whether Article I bankruptcy judges are empowered to conduct jury trials is entirely unfounded. This case simply does not involve any question as to whether Petitioners were unconstitutionally denied their Seventh Amendment right to a trial by jury.

II. THE COURT OF APPEALS CORRECTLY APPLIED THE DOCTRINE OF RES JUDICATA TO THE CLAIMS OF PETITIONERS SCPI, SANDERS, AND KREISSL AND ITS DECISION THAT THE FSI CONFIRMATION ORDER BARS CLAIMS WHICH WOULD HAVE BEEN "NON-CORE" IF ASSERTED THEREIN IS IN ACCORD WITH THE JURISDICTIONAL GRANT TO THE DISTRICT COURTS OVER ALL MATTERS RELATED TO BANKRUPTCY CASES.

While Petitioners have attempted to grab the Court's attention by trumpeting that this case purportedly involves the "bankruptcy jury trial" question, their real dispute with the court of appeals is its conclusion that, because their claims were clearly related to the FSI chapter 11 case, Petitioners should have asserted those claims in that case. However, the court of appeals' decision in this regard is in accord with the *res judicata* decisions rendered by the other courts of appeal in the bankruptcy context. Thus, because the courts of appeals' decision is not in conflict with any decision of this Court and does not conflict with any decision of

the circuit courts, there is no *res judicata* issue presented by Petitioners which would warrant granting their Petition.

Under the doctrine of *res judicata*, a final judgment on the merits bars parties or their privies from relitigating issues which were or could have been raised in a prior lawsuit involving the same transactions. *See Federated Dept. Stores, Inc. v. Moitie*, 452 U.S. 394, 398 (1981); *Chicot County Drainage Dist. v. Baxter State Bank*, 308 U.S. 371, 377-78 (1940). As long as the court which rendered the judgment had jurisdiction, even an erroneous determination is *res judicata* and not subject to collateral attack. *Stoll v. Gottlieb*, 305 U.S. 165, 172 (1938). *Res judicata* promotes finality of judgments, increases certainty, discourages multiple litigation, and conserves judicial resources. *See King v. South Central Bell Tel. & Tel. Co.*, 790 F.2d 524, 528 (6th Cir. 1986). Additionally, the application of *res judicata* to claims which could have been brought during a chapter 11 case is especially important because "[a] strong interest to achieve *finality* pervades Chapter 11 arrangements." *Oneida Motor Freight Inc. v. United Jersey Bank*, 848 F.2d 414, 417 (3d Cir.)(citation omitted) (emphasis added), *cert. denied*, 488 U.S. 967 (1988).

In its Opinion, the court of appeals in this case correctly set forth the four elements of *res judicata:*

> "1. A final decision on the merits in the first action by a court of competent jurisdiction;
>
> 2. The second action involves the same parties, or their privies, as the first;
>
> 3. The second action raises an issue actually litigated or which should have been litigated in the first action;
>
> 4. An identity of the causes of action."

973 F.2d at 480 (citations omitted).

Petitioners SCPI, Sanders, and Kreissl have not requested that this Court review any question as to whether the Confirmation Order entered by the bankruptcy court in the FSI chapter 11

case was a final judgment or whether they were parties to the FSI Chapter 11 case. Rather, Petitioners argue, *albeit* obliquely, that they should not have been required by the courts below to bring their "non-core" claims in the FSI chapter 11 case even though those claims were clearly related to that case. However, Petitioners' argument misses the mark. The doctrine of *res judicata* bars all claims which either were or *could have* been brought in the prior proceeding. Because Petitioners' claims were clearly related to the FSI chapter 11 case, they *could have* been asserted therein because 28 U.S.C. §1334(b) vests jurisdiction over all civil bankruptcy proceedings in the district courts, including their bankruptcy units. *See* 28 U.S.C. §151. The "procedures" which allocate jurisdiction over bankruptcy cases between the district courts and their bankruptcy units which are set forth in 28 U.S.C. §157 do not diminish the general bankruptcy jurisdiction granted to the district courts under section 1334(b). Therefore, Petitioners' "non-core" claims could have been first asserted in the FSI chapter 11 case. Petitioners do not, and cannot, suggest that they did not have every opportunity to assert their claims against Respondents in the FSI chapter 11 case but, for whatever tactical reasons, intentionally chose not to do so. This tactical choice now bars SCPI, Sanders, and Kreissl from asserting their claims in this case.

At least two circuit courts of appeal are in accord with the Sixth Circuit's reasoning on this issue. *See Sure-Snap Corp. v. State Street Bank & Trust Co.*, 948 F.2d 869 (2d Cir. 1991); *Eubanks v. F.D.I.C.*, 977 F.2d 166 (5th Cir. 1992). Further, the court of appeals' decision in this case does not conflict with the Seventh Circuit's decision in *Barnett v. Stern*, 909 F.2d 973 (7th Cir. 1990). Because Petitioners SCPI, Sanders, and Kreissl clearly consented to the bankruptcy court's jurisdiction in the FSI chapter 11 case by extensively participating in the proceedings which occurred therein, as set forth above, even in the Seventh Circuit, Petitioners' "non-core" claims would be barred by *res judicata*. *See In the Matter of Kroner*, 953 F.2d 317, 321 (7th Cir. 1992). Therefore, because the Sixth Circuit's decision does not conflict with any other circuit court decision which has addressed the issue of whether the doctrine of *res judicata* bars all claims which are related to a chapter 11 case when the parties

have consented to the bankruptcy court's jurisdiction, the Court should deny the Petition for this reason as well.

III. THE COURT OF APPEALS CORRECTLY DECIDED THAT, DESPITE HIS EXTENSIVE ALLEGATIONS IN THE DISTRICT COURT, PETITIONER MERIGIAN FAILED TO STATE A CLAIM OF CONTROLLING PERSON LIABILITY AGAINST HELLER UNDER THE FEDERAL SECURITIES LAWS.

Petitioner Merigian requests that the Court grant review on only one question which was decided by the court of appeals: whether Heller's administering of its loan to FSI subjects Heller to "controlling person" liability under Section 12(2) of the 1933 Securities Act, 15 U.S.C. §77l(2), or Section 10(b) of the 1934 Securities Exchange Act, 15 U.S.C. §78j. While noting that there is some disagreement among the circuit courts regarding the test for determining liability as a "controlling person" under the federal securities laws, the court of appeals in this case determined that, even under the most liberal pleading standards set forth in *Metge v. Baehler*, 762 F.2d 621 (8th Cir. 1985), *cert. denied*, 474 U.S. 1057 (1986), Merigian still failed to state a "controlling person" claim in the district court because he failed to allege that "Heller 'actually participated in the operations' of SCPI, other than by making secured loans" to FSI. *See* 973 F.2d at 485-86. By his Petition, Merigian essentially requests that this Court formulate a new legal test for determining when a lender can be a "controlling person" under the federal securities laws — a test which is not currently utilized in any of the courts of appeal. The Court should properly reject Merigian's invitation because he has presented no compelling reason why the test used by the court of appeals in this case is not in accord with prior decisions of this Court, with the decisions of the other courts of appeal, or with Congress' legislative intent when it enacted the federal securities laws.

As stated by the court of appeals in this case, a control relationship necessary to subject a lender to "controlling person"

liability under the federal securities laws requires, at a minimum, that the defendant actually participate in, *i.e.*, exercise control over, the operations of the allegedly "controlled" person and that the defendant possess the power to control the specific transactions or activities upon which the primary violation is predicated. 973 F.2d at 486. *See Schlifke v. SeaFirst Corp.*, 866 F.2d 935, 949 (7th Cir. 1989) (citing *Metge v. Baehler*, 762 F.2d 621 (8th Cir. 1985), *cert. denied*, 474 U.S. 1057 (1986)). The court of appeals correctly determined that Merigian failed to adequately allege in the district court a "controlling person" claim under the federal securities laws because "[e]xtending a loan to a company and taking measures to secure that loan do not amount to actual control." 973 F.2d at 486. This conclusion is in accord with the decisions of the other circuit courts which have considered "controlling-person" claims in the context of a debtor/creditor relationship and is supported by the law and sound policy reasons as well. Therefore, the court of appeals' decision on this issue does not warrant review by this Court.

CONCLUSION

For the foregoing reasons, the Petition for a writ of certiorari should be denied.

Respectfully submitted,

Norman H. Nachman
Counsel of Record
WINSTON & STRAWN
35 West Wacker Drive
Chicago, Illinois 60601
(312) 558-5600
Attorney for Respondents

Of Counsel:
Dan K. Webb
Gerald F. Munitz
Timothy J. Rivelli
Peter C. McCabe III
WINSTON & STRAWN
35 West Wacker Drive
Chicago, Illinois 60601
(312) 558-5600

APPENDIX A

LF

CF 10398

STATE OF MICHIGAN
DEPARTMENT OF PUBLIC HEALTH

CERTIFICATE OF DEATH

STATE FILE NUMBER
0431678

1. DECEDENT'S NAME (First, Middle, Last) SAM JOHN MERIGIAN		2. SEX MALE	3. DATE OF DEATH (Month, Day, Year) NOVEMBER 18, 1991
4a. AGE - Last Birthday (Years) 63	4b. UNDER 1 YEAR Months / Days	4c. UNDER 1 DAY Hours / Minutes	5. DATE OF BIRTH (Month, Day, Year) MARCH 29, 1928	6. COUNTY OF DEATH WAYNE
7a. LOCATION OF DEATH (Name of facility - if not in a facility, give street and number) HENRY FORD HOSPITAL		7b. IF INSIDE CITY LIMITS, SPECIFY EMERGENCY ROOM	7c. CITY, VILLAGE OR TOWNSHIP OF DEATH DETROIT
8. SOCIAL SECURITY NUMBER 374 26 3153	9a. USUAL OCCUPATION (Give kind of work done during most of working life. Do not use retired) PERSONNEL DIRECTOR		9b. KIND OF BUSINESS OR INDUSTRY GOVERNMENT
10a. USUAL RESIDENCE (Where deceased lived) STATE MICHIGAN	10b. COUNTY WAYNE	10c. INSIDE CITY LIMITS? ☒ YES ☐ NO If yes, CITY OR TOWNSHIP OF HIGHLAND PARK	10d. STREET AND NUMBER 150 PURITAN
10e. ZIP CODE 48203	11. MARRIAGE (Only one; give current or former husband or wife) HIGHLAND PARK MICHIGAN	12. MARITAL STATUS (Married, Never Married, Widowed, Divorced) MARRIED	13. SURVIVING SPOUSE (If wife, give name before first marriage) DIANNE M. ZYSKOWSKI	14. WAS DECEDENT EVER IN U.S. ARMED FORCES? YES
15. RACE - American Indian, Black, White, etc. ARMENIAN	16. DECEDENT OF HISPANIC ORIGIN? (Specify No, Yes - Mexican, Puerto Rican, Cuban, Central or South American, Other Hispanic, Not Hispanic) WHITE	17. EDUCATION (Specify only highest grade completed) Elementary/Secondary (0-12)	College (13-17 or more)
18. FATHER'S NAME (First, Middle, Last) JOHN SAM MERIGIAN		19. MOTHER'S NAME (First, Middle, Last, Before First Marriage) ZYKOCUHY KEOSHEKASHIAN	
20a. INFORMANT'S NAME (Type or Print) DIANNE M. MERIGIAN	20b. MAILING ADDRESS (Street and Number or Rural Route Number, City or Town, State, Zip Code) 150 PURITAN, HIGHLAND PARK, MICHIGAN 48203		
21. METHOD OF DISPOSITION (Burial, Cremation, Removal, Donation, Other (Specify)) BURIAL	22. PLACE OF DISPOSITION (Name of Cemetery, Crematory, or other place) EVERGREEN CEMETERY	23. LOCATION (City or Town, State) DETROIT, MICHIGAN	
24. SIGNATURE OF FUNERAL SERVICE REPRESENTATIVE [signature]	25. LICENSE NUMBER (Of Funeral Director) 5305	26. NAME AND ADDRESS OF FACILITY EDWARD MORRISON FUNERAL HOME, INC. 836 W. MAPLE ST., ROYAL OAK, MICHIGAN 48067	

27. PART I. Enter the diseases, injuries, or complications that caused the death. Do NOT enter the mode of dying, such as cardiac or respiratory arrest, shock, or heart failure. List only one cause on each line.

IMMEDIATE CAUSE (Final disease or condition resulting in death) a. Bronchogenic carcinoma, Liver — Approximate Interval Between Onset and Death: 2 mo

Sequentially list conditions, if any, leading to the immediate cause. Enter UNDERLYING CAUSE (Disease or injury that initiated the events resulting in death) LAST

b. [blank]

c. [blank]

Part II. Other significant conditions contributing to death but not resulting in the underlying cause given in Part I

28. WAS MEDICAL EXAMINER OR CORONER CONTACTED? No

29. WERE AUTOPSY FINDINGS AVAILABLE TO COMPLETE CAUSE OF DEATH? (Yes or No)

30. PLACE OF DEATH (Hospital, Nursing Home, Residence, Other (Specify)) Henry Ford Hosp.

31. WAS CASE REFERRED TO MEDICAL EXAMINER OR CORONER? (Yes or No) Yes

32. I CERTIFY THAT DEATH OCCURRED AT THE TIME, DATE, AND PLACE AND DUE TO THE CAUSE(S) AND MANNER STATED. [signature] (MD)

Operation and Date: 11/18/91

Time of Death: 3:04 AM

Date Signed: Nov 19, 1991

33. CASE NUMBER #9362-91

34. NAME AND ADDRESS OF PERSON WHO COMPLETED CAUSE OF DEATH (Item 27) (Type or Print) STEWART E. Fraser MD 15 St. Wilkins Mile - Room Oak Mi. 48073

35. LICENSE NUMBER 025511

36. SIGNATURE OF PERSON WHO COMPLETED CAUSE OF DEATH [signature]

37. DATE SIGNED (Month, Day, Year)

38. TIME OF DEATH

39. MEDICAL EXAMINER CASE NUMBER

40. PLACE OF DEATH (If other than 30, specify)

41. LOCATION (Name of City, Village or Township) (Zip Code)

42. REGISTRAR'S SIGNATURE Gloria J. Harper

43. DATE FILED (Month, Day, Year) NOV 19 1991

THIS CERTIFIES THAT THE ABOVE IS A TRUE COPY OF FACTS RECORDED ON THE RECORD OF THE PERSON NAMED HEREON, AS FILED AT THE DETROIT DEPARTMENT OF HEALTH.

Gloria J. Harper
GLORIA J. HARPER
REGISTRAR, VITAL RECORDS
DETROIT DEPARTMENT OF HEALTH

DEC 11 1992
DATED

Coleman A. Young, Mayor
City of Detroit

THE BACK OF THIS DOCUMENT CONTAINS AN ARTIFICIAL WATERMARK — HOLD AT AN ANGLE TO VIEW

BEST AVAILABLE COPY